



A REPORT
TO THE
MONTANA
LEGISLATURE

FINANCIAL AUDIT

*The University of
Montana
A Component Unit of
the State of Montana*

*For the Fiscal Year Ended
June 30, 2007*

NOVEMBER 2007

LEGISLATIVE AUDIT
DIVISION

07-10

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FINANCIAL AUDITS

Financial audits are conducted by the Legislative Audit Division to determine if the financial statements included in this report are presented fairly and the agency has complied with laws and regulations having a direct and material effect on the financial statements. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

Government Auditing Standards, the Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports. This individual agency audit report is not intended to comply with these requirements and is therefore not intended for distribution to federal grantor agencies. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2007, will be issued by March 31, 2008. The Single Audit Report for the two fiscal years ended June 30, 2005, was issued on March 6, 2006. Copies of the Single Audit Report can be obtained by contacting:

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LEGISLATIVE AUDIT DIVISION

Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor



Deputy Legislative Auditors:
James Gillett
Angie Grove

November 2007

The Legislative Audit Committee
of the Montana State Legislature:

This is our financial audit report on The University of Montana's consolidated financial statements for the fiscal year ended June 30, 2007. The statements include comparative information for the fiscal year ended June 30, 2006. The statements include component unit financial information as required under Governmental Accounting Standards Board Statement No. 39.

The university requests annual financial audits to provide timely audited financial statements to interested parties. The objective of our audit was to determine if the university's financial statements present fairly its financial position, changes in financial position, and cash flows as of June 30, 2007, and for the fiscal year then ended. This objective included determining the university's compliance with laws and regulations having a direct and material impact on the financial statements. Our opinions for fiscal year 2005-06 is based on the audit we performed in the fall of 2006.

This financial audit is a component of the biennial financial-compliance audit. Financial and financial-related audits are combined for a two-year period to constitute the financial-compliance audit. We issue the financial-related audit every other year and a financial audit every year. The financial-related audit was issued in October 2007.

The University of Montana consists of campuses located in Missoula, Butte, Dillon, and Helena. The campuses are accredited by the Commission on Colleges of the Northwest Association of Schools and Colleges and provide a diversity of programs to students.

The University of Montana-Missoula is a comprehensive university offering four-year undergraduate programs along with master and doctoral graduate programs. It includes professional schools and significant research activities. The campus is the center of liberal arts education in the Montana University System and operates the only law school in the system. Other schools include business administration, education, fine arts, forestry, pharmacy and allied health services, and journalism. In addition, the campus includes a two-year college of technology that provides a broad range of technical and occupational education and training courses.

Montana Tech of The University of Montana provides a variety of four-year and graduate programs with a focus on mineral, geological, environmental, petroleum, mining, and other engineering and science programs and majors. It also includes a college of technology that provides two-year degrees in various occupational and technical programs and core education courses.

The University of Montana-Western provides both two-year and four-year undergraduate degree programs with a focus on elementary and secondary education. It also provides a four-year liberal arts degree with several emphases that complement the education programs.

The University of Montana-Helena College of Technology provides two-year Associate of Science degree programs and a variety of other occupational, technical, and training specialties. These areas include accounting technology, carpentry, computer technology, practical nursing, electronics technology, and welding technology. The college serves as a higher education center by offering certain courses transferable to degree programs offered at other campuses of the Montana University System.

A list of Appointed and Administrative Officials having oversight responsibilities with respect to The University of Montana can be found on page i.

Beginning on page A-1, you will find the Independent Auditor's Report followed by the university's financial statements and accompanying notes. We issued an unqualified opinion on the university's consolidated financial statements, which means the reader can rely on the presented information.

This report does not contain any recommendations to the university. Any audit issues identified during this audit have been discussed with university management. The university's response to this report is on page B-1.

We thank President Dennison and his staff for their cooperation and assistance during the audit.

Respectfully submitted,

/s/ Scott A. Seacat

Scott A. Seacat
Legislative Auditor

APPOINTED AND ADMINISTRATIVE OFFICIALS

Board of Regents of Higher Education

Lynn Morrison-Hamilton, Chairman

Stephen M. Barrett, Vice Chairman

Clayton Christian

Heather O'Loughlin, Student Regent

Dr. Janine Pease

Mark Semmens

Lila Taylor

Sheila M. Stearns, Commissioner of Higher Education*

Brian Schweitzer, Governor*

Linda McCullough, Superintendent of Public Instruction*

*Ex officio members of the Board of Regents

Commissioner of Higher Education

Sheila M. Stearns Commissioner of Higher Education

Roger Barber Deputy Commissioner for Academic and Student Affairs

Mick Robinson Associate Commissioner for Fiscal Affairs

Cathy Conover Interim Associate Commissioner for Research, Technology and Communications

Frieda Houser Director, Accounting and Budgeting

Cathy Swift Chief Legal Counsel

The University of Montana, All Campuses

George M. Dennison President

The University of Montana-Missoula

George M. Dennison Vice President, Academic Affairs and University Provost

Robert Duringer Vice President for Administration and Finance, University Vice President

Daniel J. Dwyer Vice President for Research and Development, University Vice President

Teresa S. Branch Vice President for Student Affairs, University Vice President

	David Aronofsky	Legal Counsel
	Mark Pullium	Director of Business Services
Montana Tech of The University of Montana	W. Franklin Gilmore	Chancellor and University Executive Vice President
	Susan B. Patton	Vice Chancellor for Academic Affairs and Research, University Associate Provost
	Joseph F. Figueira	Vice Chancellor for Research, Graduate Studies, and University Associate Vice President
	John C. Badovinac	Controller/ Business Manager
	Carleen Cassidy	Director of Contracts and Grants
The University of Montana-Western	Richard Storey	Chancellor, University Executive Vice President
	Karl E. Ulrich	Provost and Vice Chancellor for Academic Affairs
	Susan D. Briggs	Vice Chancellor for Administration and Finance, University Associate Vice President
	Virginia Dale	Controller
The University of Montana-Helena College of Technology	Daniel Bingham	Dean/CEO
	Brandi Foster	Associate Dean for Academic Affairs
	Russ Fillner	Assistant Dean for Fiscal and Plant Operations
	Victoria Glass	Director of Financial Aid

For additional information concerning The University of Montana, contact:

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Scott A. Seacat, Legislative Auditor
Tori Hunthausen,
Chief Deputy Legislative Auditor



Deputy Legislative Auditors:
James Gillett
Angie Grove

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Consolidated Statements of Net Assets of The University of Montana, a component unit of the state of Montana, as of June 30, 2007, and 2006, and the related Consolidated Statements of Revenues, Expenses and Changes in Net Assets and Consolidated Statements of Cash Flows for the fiscal years then ended and the University Component Units - Combined Statements of Financial Position as of June 30, 2007, and 2006, and the related University Component Units - Combined Statements of Activities for the fiscal years then ended. The information contained in these financial statements is the responsibility of the university's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the university's aggregate discretely presented component units. Those statements, which include The University of Montana Foundation, the Montana Tech Foundation, The University of Montana-Western Foundation, and the Montana Grizzly Scholarship Association, were audited by other auditors whose reports thereon have been furnished to us, and our opinion insofar as it relates to the amounts included for the component units of the university, as noted above, are based on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of The University of Montana and the aggregate discretely presented component units as of June 30, 2007, and 2006, and the respective changes in financial position and cash flows, where applicable, for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis on pages A-3 through A-12 is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the basic financial statements of The University of Montana. The Supplemental Information - All Campuses on page A-44 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Respectfully submitted,

/s/ James Gillett

James Gillett, CPA
Deputy Legislative Auditor

November 8, 2007

**The University of Montana's
Management's Discussion and Analysis,
Financial Statements, Notes, and
Supplemental Information**

THE UNIVERSITY OF MONTANA

THE UNIVERSITY OF MONTANA - MISSOULA

THE UNIVERSITY OF MONTANA - WESTERN

THE UNIVERSITY OF MONTANA - HELENA COLLEGE OF TECHNOLOGY

MONTANA TECH OF THE UNIVERSITY OF MONTANA

MANAGEMENT'S DISCUSSION AND ANALYSIS

FISCAL YEAR ENDED JUNE 30, 2007

OVERVIEW

The University of Montana (University) is comprised of four campuses: The University of Montana - Missoula; The University of Montana - Western; The University of Montana - Helena College of Technology; and Montana Tech of The University of Montana. This discussion addresses the consolidated financial statements for the four campuses, and included are three basic statements: the Statement of Net Assets; the Statement of Revenues, Expenses, and Changes in Net Assets; and the Statement of Cash Flows.

The discussion and analysis which follows provides a comparative overview of the University's financial position and operating results for the fiscal years ended June 30, 2007, 2006, and 2005 and should be read in conjunction with the fiscal year 2007 financial statements.

FINANCIAL HIGHLIGHTS

The financial highlights for fiscal year 2007 were:

- Tuition rate increases for the year ended June 30, 2007 were 7% for the Western campus 8% for the Missoula campus, 10% for the Montana Tech campus, and 4% for all of our Colleges of Technology. The total tuition revenue increase for all four campuses, net of scholarship allowances, for the 2007 fiscal year was nearly \$8.0 million.
- Investment earnings increased by \$2.8 million over the prior year. The significant increase can be attributed primarily to a \$1.7 million increase in fair value of pooled equity investments. Higher federal funds rates achieved in the prior years were sustained through FY 07, which helped ensure that earnings on interest bearing investments would stay at the same level as in the prior year or increase. An additional factor contributing to the increase in investment earnings was the continued investment of approximately \$16.6 million of Series J bond proceeds, which were held in various interest bearing investments during the year.
- Long term obligations and advances from primary government decreased by \$6.6 million. Significantly, no additional long term debt was issued by the University in FY 07.
- Net assets of the University increased by \$24.1 million attributed primarily to capital grants and gifts of \$5.6 million related to the Donaldson Building addition on the Helena campus and an increase in investment earnings.
- Considerable attention was given during FY 04 to a deficit experienced by the UM Athletics Department at the Missoula campus. A plan was put in place to eliminate the accumulated deficit in the Athletics Department within five years. During FY 07, Athletics continued to exceed the targets established by the plan and eliminated the \$192,626 deficit remaining at June 30, 2006, two years earlier than planned.

The financial highlights for fiscal year 2006 were:

- On September 15, 2005, the Board of Regents (Board) and the University issued \$31,095,000 of Facilities Improvement Bonds, Series J 2005. Over \$21 million of the proceeds from the issuance, combined with certain other funds and monies of the Board and the University, are being used primarily to finance or refinance the costs of acquiring, constructing, furnishing, equipping, renovating, improving or repairing certain University facilities. The remaining \$10 million of bond proceeds were used to advance refund a portion of Facilities Improvement Bonds, Series F 1999.
- The University entered into a forward swap agreement in August, 2005 with Wachovia Bank to hedge the interest rate risk associated with the potential future issuance of \$47 million of variable-rate Series K 2010 revenue bonds. The proceeds from this issuance will be used to refund the remaining outstanding Series F 1999 revenue bonds. In exchange, the University received \$2,094,500 from Wachovia. Under the terms of the swap, the University will pay Wachovia a fixed rate substantially equal to the unrefunded Series F 1999 bonds, and Wachovia Bank will pay the University a floating rate based on the LIBOR rate. The intention of the University in entering into these transactions is to reduce the cost of its borrowings.
- Net assets of the University increased by \$16.4 million due primarily to an increase in private gifts income of \$5.8 million associated with several capital projects on the Missoula campus, and an increase in investment earnings.
- Tuition rate increases for the year ended June 30, 2006 were 7% for the Western campus, 8% for the Missoula campus, 12% for the Montana Tech campus, and 4% for all of our Colleges of Technology. The total tuition revenue increase for all four campuses, net of scholarship allowances, for the 2006 fiscal year was nearly \$4.2 million.
- Investment earnings increased by \$2.6 million over the prior year. The significant increase can in part be attributed to continued higher yields on interest bearing investments and the increase in fair value of pooled equity investments. The progressively higher federal funds rates achieved in the prior year were sustained through FY06. An additional factor contributing to the increase in investment earnings was the investment of approximately \$21 million of Series J bond proceeds, which were held in various interest bearing investments during the year.
- During FY 06, Athletics continued to exceed the targets of the deficit elimination plan, and the deficit was reduced by \$370,000 from \$562,626 at June 30, 2005 to \$192,626 at June 30, 2006.

USING THE FINANCIAL STATEMENTS

The University's financial statements consist of the following three statements: Statement of Net Assets, Statement of Revenues, Expenses and Changes in Net Assets, and Statement of Cash Flows.

A discussion of each of the individual statements follows. Some key points to be aware of regarding the statements are:

- These are consolidated financial statements representing the University's four campuses.
- The financial statements are prepared using the accrual basis of accounting, which means revenues are reported when earned, and expenses are reported when incurred.

- Assets and liabilities presented in the financial statements are generally measured at current value, although capital assets are stated at historical cost less accumulated depreciation.
- Capital assets are classified as depreciable and non-depreciable. Depreciation is treated as an operating expense.
- Assets and liabilities are treated as current (Due within one year) or as non-current (Due in more than one year), and are presented in the Statement of Net Assets in order of liquidity.
- Revenues and expenses are classified as operating or non-operating. "Operating" is defined as resulting from transactions involving exchanges of goods or services for payment, while "non-operating" is defined as resulting from transactions not involving the exchange of goods or services for payment. We show a substantial operating loss on the Statement of Revenues, Expenses, and Changes in Net Assets primarily because GASB requires that General Operating Fund expenses be reported as operating, while the State Appropriation - which is General Operating Fund revenue - must be reported as non-operating.
- Tuition and fees are reported net of any scholarships or fellowships that were applied directly to a student's account. The reason for "netting" these is to keep the University financial statements from "double counting" this revenue and expense.

STATEMENT OF NET ASSETS

The Statement of Net Assets reflects the financial position of the University at the end of the fiscal year. The changes in net assets that occur over time indicate improvements or deterioration in the University's financial position. A summary of the Statement of Net Assets follows:

For the years ended June 30, (stated in millions)			
Description	2007	2006	2005*
Total current assets	\$ 109.54	\$ 106.40	\$ 85.03
Total non-current assets	301.75	283.88	272.97
Total assets	\$ 411.29	\$ 390.28	\$ 358.00
Total current liabilities	\$ 47.30	\$ 44.49	\$ 45.46
Total non-current liabilities	169.59	175.54	158.64
Total liabilities	216.89	220.03	204.10
Invested in Capital Assets, Net of Related Debt	134.28	119.58	105.95
Restricted:			
Nonexpendable	21.07	17.83	15.68
Expendable	5.50	5.54	5.31
Unrestricted	33.55	27.30	26.96
Total net assets	194.40	170.25	153.90
Total liabilities and net assets	\$ 411.29	\$ 390.28	\$ 358.00

*Restated

Events or developments that occurred which had a significant impact on the Statement of Net Assets include:

Events or developments which occurred during 2007:

- Non current assets increased by \$17.9 million primarily from additions to capital assets of \$30.0 million net of an increase to accumulated depreciation of \$15.8 million. A \$1.7 million increase in the fair value of long term investments also contributed to the increase in non current assets.
- Non current liabilities decreased by \$5.9 million due primarily to principal payments of \$6.4 million on outstanding revenue bonds payable, notes payable and advances from primary government. The University did not issue any additional long term debt during FY 07.
- Net assets increased by \$24.1 million due in part to a \$5.6 million of state funding related to the Donaldson Building addition on the Helena campus. In addition, investments increased by \$3.6 million, which included a \$1.6 million federal endowment.

Events or developments which occurred during 2006:

- Current assets increased by \$21.4 million, with most of that change resulting from an increase in cash and cash equivalents of \$27.3 million. Most of the increase was from Series J 2005, bond proceeds invested in highly liquid guaranteed investment contracts and will be used to pay for several major capital projects.
- Non current assets increased by \$10.9 million primarily from additions to capital assets of \$25.9 million net of an increase to accumulated depreciation of \$16.4 million.
- Non current liabilities increased by \$16.9 million due primarily to the issuance of Series J 2005 revenue bonds, which was offset by principal payments of \$5.0 million related to revenue bonds outstanding in FY06.
- Net assets of the University increased by \$16.4 million due primarily to an increase in private gifts income of \$5.8 million associated with the construction of the Skaggs and Journalism buildings on the Missoula campus and also, from an increase in investments earnings.

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

The Statement of Revenues, Expenses, and Changes in Net Assets present the results of the University's operational activities for the fiscal year, categorizing them as either operating or non-operating items. Consistent with the accrual method of accounting, the current year's revenues and expenses are recognized when they were earned or incurred, regardless of when cash was received or paid.

A summary of the Statement of Revenues, Expenses and Changes in Net Assets follows:

	For the years ended June 30,		
	(stated in millions)		
<u>Description</u>	<u>2007</u>	<u>2006*</u>	<u>2005**</u>
Operating revenues	244.49	\$ 230.15	\$ 218.18
Operating expenses	310.45	294.79	280.35
Operating loss	(65.96)	(64.64)	(62.17)

Non-operating revenues (expenses)	80.21	76.91	64.14
Income before other revenues	14.25	12.27	1.97
Other revenues	9.90	4.09	5.81
Net increase in net assets	24.15	16.36	7.78
Net assets, beginning of year, as adjusted	170.25	153.89	146.11
Net assets, end of year	\$ 194.40	\$ 170.25	\$ 153.89

*Restated

** The amounts presented do not reflect a change in the classification of graduate teaching assistant fee waivers to compensation and benefits, and the related effect of the reclassification on the amount of tuition discounting. Had the FY2005 amounts been adjusted to reflect the impact of this change, operating revenues would increase by approximately \$2.7 million and operating expenses would increase by \$2.7 million.

The following provides a comparative analysis of revenues and expenses for the years ended June 30, 2007, 2006, and 2005:

	For the years ended June 30, (stated in millions)					
	<u>2007</u>		<u>2006*</u>		<u>2005**</u>	
	Amount	Percent	Amount	Percent	Amount	Percent
REVENUES						
Tuition and fees, net	\$ 99.15	29.0%	\$ 91.17	28.6%	\$ 83.08	28.2%
Federal grants and contracts	63.92	18.7%	64.65	20.3%	65.67	22.3%
State & local grants/contracts	9.20	2.7%	8.91	2.8%	7.42	2.5%
Nongovernmental grants/contracts	6.57	1.9%	4.99	1.6%	3.99	1.3%
Facilities and administrative cost allowances	10.46	3.1%	9.79	3.1%	10.42	3.5%
Sales/services of educational departments	14.14	4.1%	12.35	3.9%	12.28	4.2%
Auxiliary enterprise charges	34.33	10.0%	32.76	10.3%	30.08	10.2%
State appropriations	63.45	18.6%	62.07	19.5%	56.70	19.2%
Investment income	8.03	2.3%	5.18	1.6%	2.57	0.9%
Private gifts	14.66	4.3%	15.58	4.9%	9.73	3.3%
Capital grants and gifts	8.15	2.4%	3.06	0.9%	5.81	2.0%
All other sources combined	9.98	2.9%	8.01	2.5%	6.98	2.4%
	<u>\$ 342.04</u>	<u>100.0%</u>	<u>\$ 318.52</u>	<u>100.0%</u>	<u>\$ 294.73</u>	<u>100.0%</u>
EXPENSES						
Compensation and benefits	\$ 201.17	63.3%	\$ 189.61	62.8%	\$ 175.85	61.2%
Other operating expenses	76.08	23.9%	73.79	24.4%	72.73	25.4%
Scholarships and fellowships	16.36	5.2%	14.68	4.9%	15.70	5.3%
Depreciation and amortization	16.84	5.3%	16.71	5.5%	16.07	5.6%
Interest expense	7.44	2.3%	7.37	2.4%	6.60	2.5%
	<u>\$ 317.89</u>	<u>100.0%</u>	<u>\$ 302.16</u>	<u>100.0%</u>	<u>\$ 286.95</u>	<u>100.0%</u>

* Restated

** The amounts presented do not reflect a change in the classification of graduate teaching assistant fee waivers to compensation and benefits, and the related effect of the reclassification on the amount of tuition discounting. Had the FY2005 amounts been adjusted to reflect the impact of this change, tuition and fees, net, would increase by approximately \$2.7 million, compensation and benefits would increase by \$3.3 million, and scholarships and fellowships would decrease by a net amount of \$638 thousand.

Comments about specific revenue and expense items are:

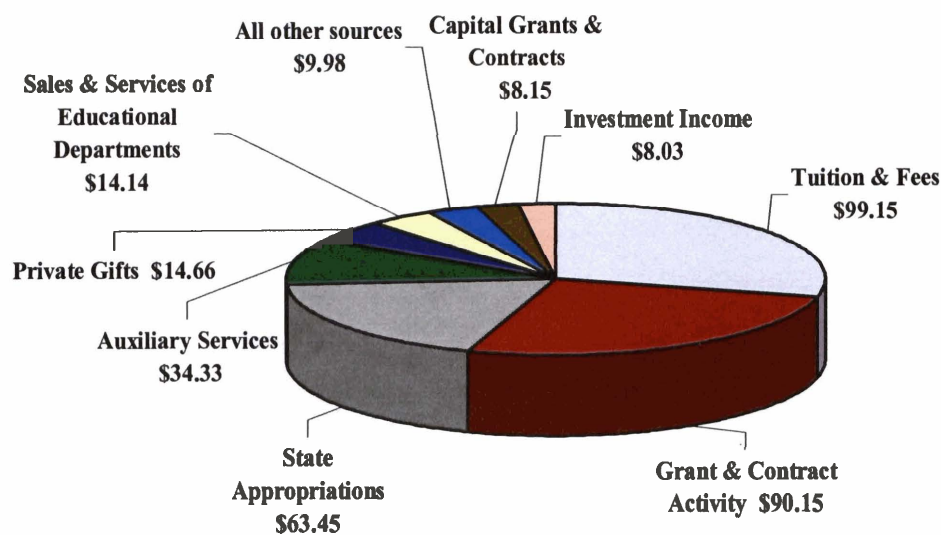
Events or developments which occurred during 2007 include:

- Tuition and fees increased by almost \$8.0 million, with approximately \$6.4 million of the increase attributable to higher tuition rates, and the remainder to higher enrollments in FY07.
- Grants and contract revenue from state, local and private funding sources, and facilities and administrative cost allowances, increased by over \$2.2 million. Funding for research from federal sources continues to be difficult to obtain because of the federal government's war effort in Iraq. As a result, funding from this source declined by almost \$734 thousand in FY 07.
- Sales and service revenue increased by almost \$1.8 million over FY 06, with approximately \$1.0 million of the increase attributable to additional intercollegiate athletics event ticket sales and game guarantees, and additional special event ticket sales. An increase in educational department sales and service revenue accounts for most of the remaining increase.
- Investment earnings increased by over \$2.8 million due largely to a \$1.7 million fair value increase in pooled equity investments. The investment earnings were also positively impacted by the investment of over \$17.1 million of unexpended bond proceeds in various interest bearing investments throughout the year, as well as continued higher yields on the State's Short Term Investment Pool (STIP). STIP rates averaged 4.25% in 2006 and 5.35% in 2007.
- Capital grants and gifts increased by approximately \$5.1 million due primarily to \$5.6 million of State funding received for the Donaldson Building addition on the Helena campus.
- Operating expenses increased by approximately \$15.7 million due primarily to increases in salaries and benefits, and supplies and other services of approximately \$11.6 million and \$1.9 million, respectively. Salary increases in FY 07 for classified staff and faculty were 3.6% and 3.0%, respectively. Employer contributions for employee benefits including health insurance, increased by approximately 10% over FY 06.

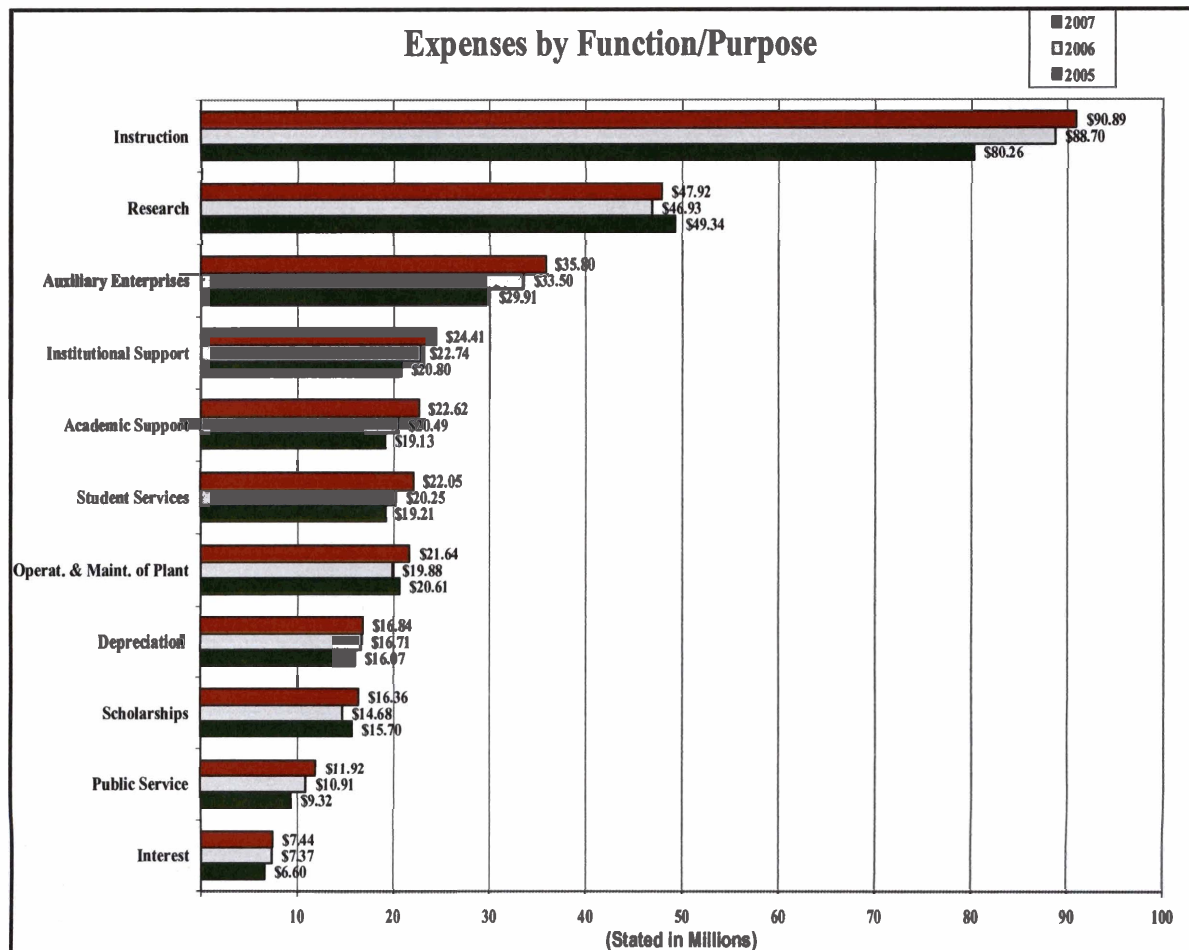
Events or developments which occurred during 2006 include:

- Tuition and fees increased by nearly \$4.9 million, with approximately \$4.2 million of the increase attributable to higher tuition rates, and the remainder to higher enrollments in FY06.
- Federal grants and contracts revenue and facilities and administrative cost allowances declined in total by over \$1.6 million in FY06, reflecting the difficulty in obtaining federal funding. The University has put more effort in obtaining state and local contracts as a result, and revenue from these sources increased by \$2.5 million.
- State appropriation increased by \$5.4 million, with about \$4.5 million attributable to an increase in funding to the Montana University System for the 2006-2007 Biennium, approved by the 2005 state legislature. The remainder of the increase is from a special appropriation for program development at our colleges of technology.
- Private gifts increased by \$5.8 million, with most of the increase from foundation donations for several capital projects on the Missoula campus.
- Investment earnings increased by \$2.6 million due to higher yields on interest bearing investments, a fairly significant increase in fair value of pooled equity investments and the investment of approximately \$21 million of Series J bond proceeds, which were held in various interest bearing investments during the year.

FY 2007
Revenues by Source = \$342.04 Million
(\$ in Millions)



Expenses by Function/Purpose



STATEMENT OF CASH FLOWS

The Statement of Cash Flows provides information about the University's sources and uses of cash during the fiscal year. This statement aids in assessing the University's ability to meet obligations and commitments as they become due, their ability to generate future cash flows, and their needs for external financing. As required by GASB, the statement is presented using the "Direct Method", which focuses on those transactions that either provided or used cash during the fiscal year.

	For years ended June 30, (stated in millions)		
	2007	2006	2005
<u>CASH FLOW CATEGORY</u>			
Cash Provided by(Used for):			
Operating Activities	\$ (47.39)	\$ (49.19)	\$ (43.95)
Non-capital Financial Activities	80.13	80.66	71.61
Capital and Related Financial Activities	(36.44)	(13.85)	(24.17)
Investing Activities	6.12	8.98	(3.06)
Net Increase in Cash	2.42	26.60	.43
Cash and Cash Equivalents, beginning of year	84.63	58.03	57.60
Cash and Cash Equivalents, end of year	\$ 87.05	\$ 84.63	\$ 58.03

Specific events or cash transactions in FY 07 which were notable included:

- Cash flows from operating revenues increased by approximately \$11.6 million over FY 06, due primarily to an increase in cash flows from tuition and fees, auxiliary enterprise charges, and sales and service activities totaling \$10.9 million. This increase in cash flows was offset by an increase in operating expenses of \$9.8 million due largely to an increase in payments for salaries and benefits of \$7.9 million.
- Cash provided by investing activities declined by \$2.8 million over the prior year due primarily to an overall decrease in the purchase and sale of investments.
- Overall, \$36.4 million in cash was used in capital and related financing activities, or an increase of \$22.6 million in comparison to FY 06. The University did not issue additional long term debt in FY 07 to finance current or future acquisitions of capital assets. In FY 07, \$22.8 million was paid for construction and acquisition of capital assets. An additional \$13.8 million of cash was used to make debt service payments on long term obligations, including, \$6.4 million of principal paid.

Specific events or cash transactions in FY 06 which were notable included:

- Cash flows from operating revenues increased by approximately \$11.0 million, due primarily to an increase in cash flows from tuition and fees and auxiliary enterprise charges totaling \$7.9 million. This increase in cash flows was offset by an increase in operating expenses of \$16.3 million due largely to an increase in payments for salaries and benefits of \$13.7 million.
- Noncapital financing activities provided additional cash flows over the prior year due to an increase in state appropriations of \$5.4 million and a significant increase in private gifts of \$5.8 million, designated primarily for use by several capital building projects.

- Cash flows provided by investing activities increased in excess of \$12.0 million over FY 05. A major reason for the increase was due to the increase in maturities of close to \$6.0 million of debt securities during the year, and a corresponding decrease in investments of \$3.3 million compared to FY 05. The proceeds from the maturity of debt securities were used to fund capital construction activities. Another factor contributing to the increase in cash flows from these activities was an increase in investment earnings of \$2.4 million, resulting from higher yields on interest bearing investments.
- Overall, cash flows from capital and related financing activities increased by \$12 million in FY06. Proceeds from the issuance of Series J 2005 bonds net of payments to defease a portion of Series F 1999 bonds, increased cash flows by \$21 million. This increase was offset by cash used for acquiring capital assets, which increased by \$8.5 million over FY 05.

DISCUSSION OF SIGNIFICANT PENDING ECONOMIC AND FINANCIAL ISSUES

The issues we view as significant pending economic or financial issues for the four campuses of the University are:

- As of June 30, 2007, a number of major construction projects were nearing completion, including, on the Missoula campus, an addition to the School of Pharmacy and Allied Health Sciences Skaggs Building (estimated cost of \$14 million), a new journalism school building, Anderson Hall (estimated cost of \$11.4 million) and on the Helena campus, an addition to the Donaldson Building (estimated cost of \$7.5 million). In addition at year end, Phase I of the expansion/upgrade of the steam distribution system on the Missoula campus (estimated cost \$9 million) was underway.

Looking ahead to the 2009 biennium, the University plans to undertake 10 major construction projects, with estimated costs in excess of \$84.5 million. The projects are as follows:

Project Name	Estimated Start Date	Estimated Cost (in millions)	Campus
Interdisciplinary Science Building	Fall, 2007	\$13.8	Missoula
McGill Hall Health & Human Performance Addition	Fall, 2007	\$1.4	Missoula
Washington-Grizzly Stadium Expansion	Winter, 2008	\$5.5	Missoula
Law School Expansion	Spring, 2008	\$14.8	Missoula
Phase II of the Steam Distribution System	Spring 2008	\$2.0	Missoula
Native American Center	Summer, 2008	\$6.0	Missoula
Gilkey Executive Education Center	Summer, 2008	\$6.0	Missoula
Phyllis Washington Education Addition	Summer, 2008	\$10.0	Missoula
MBMG/Petroleum Building	Summer, 2008	\$20.5	MT Tech
Main Hall Renovation	Fall, 2008	\$4.5	Western

These projects will be funded from a variety of sources including, Series J bond proceeds, private donations and state funding.

- The 2007 Session of the Montana Legislature did not appropriate sufficient additional funding to cover operation and maintenance costs associated with several new facilities on the Missoula campus. A concern for the University is securing long term funding to cover these ongoing costs without adversely affecting academic programs or administrative services.

- The number of high school graduates in Montana is projected to decline 17% to 19% over the next 10 years. This will likely translate into a significant decrease in the number of new resident students who will enroll at the University each year during this time period. To help mitigate the impact of future enrollment declines, the University has or will be implementing a number of long term strategies to improve access and retention of this smaller pool of in-state students. While tuition at the University is in the moderate range when compared to other peer institutions, even a moderate level of tuition increase is not affordable for many Montana families. To improve access and hopefully increase the participation rate of a smaller pool of prospective in-state students, the University will continue to refine such programs as Montana Partnering for Affordable College Tuition (MPACT) to minimize debt burden as a barrier to participation. The University will also continue to encourage more need-based assistance at the State level to help increase the overall support provided to economically disadvantaged students. An initiative is currently underway to develop and implement a responsive retention program to improve the retention rate of freshmen through sophomore students.

Other efforts by the University to mitigate declining resident enrollment include broadening marketing efforts to attract more non-resident students, including foreign students. In addition, the University has placed emphasis on graduate enrollments and research involvement.

- The 2007 Session of the Montana Legislature approved a plan proposed by the Governor to freeze tuition for Montana resident students during the two years of the 2009 biennium. The Governor's initiative is known as the College Affordability Plan (CAP). The CAP replaced tuition revenue with general fund appropriation. The Governor's plan is a welcome relief for Montana students after an extended period of rising tuition. Nonresident student tuition and mandatory fees are not frozen and can be increased during the biennium upon approval by the Board of Regents.
- The University continues to seek ways to improve the efficiency and effectiveness of its operations through an on-going assessment of its business practices. It must pursue initiatives to generate additional financial support, reduce operating costs, while improving services to students.

The University of Montana
A Component Unit of the State of Montana
Consolidated Statements of Net Assets
As of June 30, 2007 and 2006

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	2007	2006
ASSETS		
Current Assets		
Cash and cash equivalents (note 3)	\$ 86,849,768	\$ 84,427,472
Securities lending collateral	317,923	836,492
Investments	270,530	1,801,141
Accounts and grants receivable, net	5,672,296	4,452,194
Due from Federal government	7,756,875	7,803,785
Due from primary government	2,343,985	1,669,790
Due from other State of Montana component units	392,099	428,548
Loans to students, net	1,626,004	1,564,564
Inventories	1,802,423	1,759,980
Prepaid expenses and deferred charges	2,505,436	1,661,508
Total current assets	\$109,537,339	\$106,405,474
Noncurrent Assets		
Restricted cash and cash equivalents	\$ 206,554	\$ 204,516
Restricted investments	21,013,235	17,390,643
Other long term investments	5,891,682	6,075,053
Loans to students, net	9,040,653	9,664,456
Bond issuance costs	2,152,611	2,269,912
Capital assets, net	263,444,684	248,272,379
Total Noncurrent Assets	\$301,749,419	\$283,876,959
Total Assets	\$411,286,758	\$390,282,433
LIABILITIES		
Current Liabilities		
Accounts payable and accrued liabilities	\$ 15,603,574	\$ 14,527,916
Due to Federal government	53,937	150
Due to primary government	924,390	815,573
Due to other State of Montana component units	38,678	24,027
Securities lending liability	317,923	836,492
Student and other deposits	2,642,572	2,290,565
Deferred revenue	13,238,008	12,503,336
Accrued compensated absences	8,290,619	7,763,180
Current portion of long-term obligations	6,179,874	5,725,342
Total Current Liabilities	\$ 47,289,575	\$ 44,486,581
Noncurrent Liabilities		
Accrued compensated absences	\$ 12,099,491	\$ 11,596,372
Long term obligations	140,303,151	146,509,434
Advances from primary government	5,076,359	5,466,479
Due to Federal Government	10,020,616	9,875,660
Derivative financial instrument	2,094,500	2,094,500
Total Noncurrent Liabilities	\$169,594,117	\$175,542,445
Total Liabilities	\$216,883,692	\$220,029,026
NET ASSETS		
Invested in capital assets, net of related debt	\$134,280,592	\$119,572,500
Restricted for:		
Nonexpendable		
Endowments	19,159,970	15,958,648
Loans	1,909,185	1,874,706
Expendable		
Loans	1,897,207	1,698,933
Scholarships, research, instruction, and other	3,604,149	3,850,034
Unrestricted	33,551,963	27,298,586
Total Net Assets	\$194,403,066	\$170,253,407
Total Liabilities & Net Assets	\$411,286,758	\$390,282,433

The accompanying notes are an integral part of these financial statements.

The University of Montana

A Component Unit of the State of Montana

University Component Units - Combined Statements of Financial Position

As of June 30 or December 31, 2007 and 2006

	2007	2006
ASSETS		
Cash and cash equivalents	\$ 10,223,009	\$9,646,463
Short-term investments	7,607,602	10,081,974
Accrued dividends and interest	348,277	354,288
Investments	177,388,895	146,820,969
Contributions receivable, net	15,877,321	17,685,297
Contracts and notes receivable, net	258,714	31,393
Student loans and other receivables	252,976	186,619
Depreciable assets, net of accumulated depreciation	4,709,350	4,949,334
Other assets	706,747	518,232
Total Assets	\$ 217,372,891	\$ 190,274,569
LIABILITIES		
Accounts payable	\$ 152,747	\$ 58,417
Accrued expenses	27,436	27,150
Compensated absences	179,168	168,944
Note payable - bank	609,873	469,614
Note payable - long-term	57,453	75,712
Liabilities to external beneficiaries	2,904,226	2,786,406
Custodial funds	24,353,157	19,582,375
Other liabilities	247,319	316,896
Total Liabilities	\$ 28,531,379	\$ 23,485,514
NET ASSETS		
Net assets - unrestricted	11,175,235	10,450,806
Net assets - temporarily restricted	78,254,364	63,864,257
Net assets - permanently restricted	99,411,913	92,473,992
Total Net Assets	\$ 188,841,512	\$ 166,789,055
Total Liabilities & Net Assets	\$ 217,372,891	\$ 190,274,569

The accompanying notes are an integral part of these financial statements.

The University of Montana

A Component Unit of the State of Montana

Consolidated Statements of Revenues, Expenses and Changes in Net Assets

For the Years Ended June 30, 2007 and 2006

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	2007	2006*
OPERATING REVENUES:		
Tuition and fees (net of scholarship allowances in 2007 and 2006 of \$17,949,275 and 17,713,186, respectively; 2007 and 2006 revenues of \$11,292,252 and \$11,083,016 respectively, are pledged)	\$ 99,151,493	\$ 91,169,556
Federal grants and contracts	63,916,568	64,650,157
State and local grants and contracts	9,198,949	8,913,433
Nongovernmental grants and contracts	6,569,106	4,984,611
Grant and contract facilities and administrative cost allowances	10,456,648	9,793,983
Sales and services of educational departments (2007 and 2006 revenues of \$4,057,684 and \$3,562,413, respectively, are pledged)	14,138,787	12,347,010
Auxiliary enterprises charges:		
Residential life (net of scholarship allowances in 2007 and 2006 of \$1,213,061 and \$923,263, respectively; 2007 and 2006 revenues of \$12,365,385 and \$11,876,485, respectively, are pledged)	12,373,989	11,930,935
Food services (net of scholarship allowances in 2007 and 2006 of \$1,213,061 and \$923,263, respectively; 2007 and 2006 revenues of \$10,491,524 and \$9,717,646 respectively, are pledged)	10,492,514	9,899,853
Other auxiliary revenues (2007 and 2006 revenues of \$10,385,865 and \$9,692,759, respectively, are pledged)	11,460,009	10,924,707
Interest earned on loans to students	46,005	47,480
Other operating revenues	6,689,346	5,482,745
Total operating revenues	\$ 244,493,414	\$230,144,470
OPERATING EXPENSES:		
Compensation and employee benefits	\$ 201,174,968	\$189,608,103
Other (note 18)	76,078,147	73,785,705
Scholarships and fellowships	16,355,573	14,682,460
Depreciation and amortization	16,842,365	16,710,382
Total operating expenses	\$ 310,451,053	\$294,786,650
OPERATING LOSS	\$ (65,957,639)	\$ (64,642,180)
NON-OPERATING REVENUES (EXPENSES):		
State appropriations	\$ 63,455,247	\$ 62,073,958
Land grant revenues (revenues are pledged)	1,505,512	1,452,867
Private gifts	14,661,178	15,575,156
Investment income (2007 and 2006 revenues of \$2,831,339 and \$2,005,526, respectively, are pledged)	8,033,742	5,184,299
Interest expense	(7,442,523)	(7,376,448)
Net non-operating revenues	\$ 80,213,156	\$ 76,909,832
INCOME BEFORE OTHER REVENUES (EXPENSES)	\$ 14,255,517	\$ 12,267,652
OTHER REVENUES (EXPENSES):		
Capital grants and gifts	\$ 8,149,640	\$ 3,063,894
Additions to permanent endowments	1,562,500	1,562,500
Gain (loss) on disposal of capital assets	182,002	(538,074)
Total other revenues	\$ 9,894,142	\$ 4,088,320
Net increase in net assets	\$ 24,149,659	\$ 16,355,972
NET ASSETS:		
Net assets - beginning of year	\$ 170,253,407	\$153,897,435
Net assets - end of year	\$ 194,403,066	\$170,253,407

*Restated

The University of Montana

A Component Unit of the State of Montana

University Component Units - Combined Statement of Activities

For the Years Ended June 30 or December 31, 2007 and 2006

	Unrestricted	Temporarily Restricted	Permanently Restricted	2007 Total
REVENUES:				
Contributions	\$ 1,355,595	\$ 12,513,188	\$ 6,292,472	\$ 20,161,255
Interest and dividend income	809,943	3,602,645	-	4,412,588
Net realized and unrealized gain (loss) on investments	264,591	16,823,234	631,621	17,719,446
Loss on impairment of asset	(166,170)	-	-	(166,170)
Loss on sale of assets	(33,500)	-	-	(33,500)
Support received from university	292,000	69,500	-	361,500
Special events	599,331	253,936	86	853,353
Other income	19,395	863,254	-	882,649
Net assets released from restrictions	19,347,326	(19,347,326)	-	-
Total revenues	\$ 22,488,511	\$ 14,778,431	\$ 6,924,179	\$ 44,191,121
EXPENSES:				
Program services				
Academic and institutional	\$ 6,749,270	\$ -	\$ -	\$ 6,749,270
Capital expenses	4,755,090	-	-	4,755,090
Scholarships and awards	5,275,620	-	-	5,275,620
Total program services	\$ 16,779,980	\$ -	\$ -	\$ 16,779,980
Operating expenses				
Fundraising efforts	\$ 2,741,252	\$ -	\$ -	\$ 2,741,252
General and administrative	1,616,782	-	-	1,616,782
Investment management costs	390,578	-	-	390,578
Other miscellaneous	242,426	-	-	242,426
Total operating expenses	\$ 4,991,038	\$ -	\$ -	\$ 4,991,038
Change in net assets before nonoperating items	\$ 717,493	\$ 14,778,431	\$ 6,924,179	\$ 22,420,103
NON-OPERATING REVENUES (EXPENSES):				
Payments to beneficiaries and change in liabilities due to external beneficiaries	6,936	(374,582)	-	(367,646)
Adjustments	-	(13,742)	13,742	-
Change in net assets	\$ 724,429	\$ 14,390,107	\$ 6,937,921	\$ 22,052,457
Net assets, beginning of year	10,450,806	63,864,257	92,473,992	166,789,055
Net assets, end of year	\$ 11,175,235	\$ 78,254,364	\$ 99,411,913	\$188,841,512

The accompanying notes are an integral part of these financial statements.

The University of Montana

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A Component Unit of the State of Montana

University Component Units - Combined Statement of Activities

For the Years Ended June 30 or December 31, 2006 and 2005

	Unrestricted	Temporarily Restricted	Permanently Restricted	2006 Total
REVENUES:				
Contributions	\$ 1,514,840	\$ 16,428,098	\$ 5,037,433	\$ 22,980,371
Interest and dividend income	525,727	2,846,679	-	3,372,406
Net realized and unrealized gain (loss) on investments	36,258	8,424,993	103,665	8,564,916
Support received from university	322,800	-	-	322,800
Special events	497,163	324,833	240	822,236
Other income	18,867	692,394	-	711,261
Net assets released from restrictions	20,705,337	(20,705,337)	-	-
Total revenues	\$ 23,620,992	\$ 8,011,660	\$ 5,141,338	\$ 36,773,990
EXPENSES:				
Program services				
Academic and institutional	\$ 6,419,008	\$ -	\$ -	\$ 6,419,008
Capital expenses	7,218,676	-	-	7,218,676
Scholarships and awards	4,607,768	-	-	4,607,768
Total program services	\$ 18,245,452	\$ -	\$ -	\$ 18,245,452
Operating expenses				
Fundraising efforts	\$ 2,544,619	\$ -	\$ -	\$ 2,544,619
General and administrative	1,364,088	-	-	1,364,088
Investment management costs	186,755	-	-	186,755
Other miscellaneous	383,190	-	-	383,190
Total operating expenses	\$ 4,478,652	\$ -	\$ -	\$ 4,478,652
Change in net assets before nonoperating items	\$ 896,888	\$ 8,011,660	\$ 5,141,338	\$ 14,049,886
NON-OPERATING REVENUES (EXPENSES):				
Payments to beneficiaries and change in liabilities due to external beneficiaries	(153)	(690,413)	-	(690,566)
Adjustments	(5,210)	60,773	(55,563)	-
Change in net assets	\$ 891,525	\$ 7,382,020	\$ 5,085,775	\$ 13,359,320
Net assets, beginning of year	9,559,281	56,482,237	87,388,217	153,429,735
Net assets, end of year	\$ 10,450,806	\$ 63,864,257	\$ 92,473,992	\$ 166,789,055

The accompanying notes are an integral part of these financial statements.

The University of Montana

A Component Unit of the State of Montana

Consolidated Statements of Cash Flows

For the Years Ended June 30, 2007 and 2006

	2007	2006*
CASH FLOWS FROM OPERATING ACTIVITIES		
Student tuition and fees	\$ 98,509,824	\$ 91,273,788
Federal grants and contracts	63,975,328	66,055,452
State grants and contracts	9,187,248	9,083,207
Nongovernmental grants and contracts	6,560,751	5,079,552
Grant and contract facilities and administrative cost allowances	10,456,648	9,793,983
Sales and services of educational activities	14,556,187	12,628,702
Auxiliary enterprises charges	34,485,276	32,708,738
Interest earned on loans to students	116,174	76,751
Other operating receipts	6,228,995	5,734,091
Payments to employees for salaries and benefits	(199,839,312)	(191,907,070)
Operating expenses	(75,662,730)	(74,536,623)
Payments for scholarships and fellowships	(16,355,573)	(14,682,460)
Loans made to students	(2,401,091)	(3,735,931)
Loan payments received	2,794,572	3,238,467
Net Cash Used by Operating Activities	\$ (47,387,703)	\$ (49,189,353)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
State appropriations	\$ 63,455,247	\$ 62,073,958
Land Grants	1,505,512	1,452,867
Private Gifts	13,603,340	15,565,314
Additions to permanent endowments	1,562,500	1,572,425
Net Cash Provided by Noncapital Financing Activities	\$ 80,126,599	\$ 80,664,564
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	\$ (1,574,689)	\$ (3,638,219)
Proceeds from sales of investments	1,587,772	7,771,747
Earnings received on investments	6,112,051	4,845,171
Net Cash Provided by Investing Activities	\$ 6,125,134	\$ 8,978,699
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Cash paid for capital assets	\$ (22,804,298)	\$ (22,355,330)
Proceeds from the sale of capital assets	211,970	86,414
Proceeds from notes payable and advances from primary government	-	484,835
Principal paid on notes payable, advance from primary government, and capital leases	(1,273,114)	(1,270,725)
Principal paid on bonds payable	(5,105,000)	(5,010,000)
Principal and premium paid to defease revenue bonds	-	(11,259,479)
Proceeds from issuance of revenue bonds	-	31,205,748
Proceeds from swaption contract	-	2,094,500
Bond issuance costs paid on new issue	-	(670,417)
Interest paid on capital debt and leases	(7,469,254)	(7,153,560)
Net Cash Used by Capital and Related Financing Activities	\$ (36,439,696)	\$ (13,848,014)
Net Increase in Cash and Cash Equivalents	\$ 2,424,334	\$ 26,605,896
Cash and Cash Equivalents, Beginning of Year	\$ 84,631,988	\$ 58,026,092
Cash and Cash Equivalents, End of Year	\$ 87,056,322	\$ 84,631,988

* Restated

The University of Montana
A Component Unit of the State of Montana
Consolidated Statements of Cash Flows

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For the Years Ended June 30, 2007 and 2006

(Continued)

	2007	2006
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used By) Operating Activities:		
Operating loss:	\$ (65,957,639)	\$ (64,642,180)
Adjustments to reconcile operating loss to net cash used by operating activities		
Depreciation and amortization expense	16,842,365	16,710,382
Other amortization expense	335,920	528,415
Changes in assets and liabilities:		
Accounts receivable	(1,810,938)	(177,425)
Loans to students	562,363	(327,880)
Inventories	(42,443)	(28,568)
Prepaid expenses and deferred charges	(843,926)	(41,246)
Accounts payable and accrued expenses	1,264,402	(4,713,024)
Deferred revenue	734,672	1,903,695
Student and other deposits	352,007	295,719
Due to federal government	144,956	179,291
Compensated absences	1,030,558	1,123,468
Net Cash Used by Operating Activities	\$ (47,387,703)	\$ (49,189,353)
Noncash Investing, Noncapital Financing, and Capital and Related Financing Transactions		
Fixed assets acquired by incurring capital lease obligations	\$ (86,413)	\$ (444,297)
Change in fair value of investments recognized as a component of interest income	1,921,693	339,128
Fixed assets acquired from Capital grants and donations	8,149,640	3,063,893
Reconciliation of Cash and Cash Equivalent to the Statement of Net Assets		
Cash and cash equivalents classified as current assets	\$ 86,849,768	\$ 84,427,472
Cash and cash equivalents classified as noncurrent assets	206,554	204,516
Total Cash and Cash Equivalents, End of Year	\$ 87,056,322	\$ 84,631,988

The accompanying notes are an integral part of these financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

THE UNIVERSITY OF MONTANA

A COMPONENT UNIT OF THE STATE OF MONTANA

FOR THE YEARS ENDED JUNE 30, 2007 AND 2006

NOTE 1 – ORGANIZATION, REPORTING ENTITY AND BASIS OF PRESENTATION

▪ ORGANIZATION

The University of Montana (University) is a component unit of the State of Montana (State) with an enrollment of approximately 18,000 students on its four campuses. The State of Montana Board of Regents (Board of Regents) is appointed by the Governor of the State and has oversight responsibility with respect to the University. The State allocates and allots funds to each campus separately and requires that the funds be maintained accordingly.

▪ REPORTING ENTITY

The accompanying consolidated financial statements include all activities of the four campuses of the University, the Forestry Experiment Station and the Montana Bureau of Mines. The four campuses of the University are The University of Montana – Missoula, Montana Tech of The University of Montana, which is located in Butte, The University of Montana – Western, which is located in Dillon, and The University of Montana - Helena College of Technology.

GASB Statement No. 39, “Determining Whether Certain Organizations Are Component Units, an Amendment of GASB Statement No. 14” requires that a legally tax exempt organization should be reported as a component unit of a reporting entity if the economic resources received or held by these organizations are entirely or virtually entirely for the direct benefit of the reporting entity or its component units, and the reporting entity is entitled to, or has the means to otherwise access, a majority of the economic resources received or held by the separate organization. The resources of the separate organization must also be significant to the reporting entity. The University has established a threshold minimum of one percent of consolidated net assets or one percent of consolidated revenues as an additional requirement for inclusion of an organization as a component unit in its financial statements. In addition, other organizations should be evaluated for inclusion if they are closely related to, or financially integrated with, the reporting entity. All component units and other related organizations will be tested and evaluated on an annual basis for inclusion under GASB No. 39. Accordingly, the University has identified and will present the combined activities of four component units, The University of Montana Foundation, The Montana Tech Foundation, The University of Montana - Western Foundation, and the Montana Grizzly Scholarship Association. For further discussion of accounting for component units, see Consolidated Financial Statements Note 19, “Accounting for Component Units.”

The University is considered a component unit of the State of Montana under GASB No. 14. As such, the financial statements for the University are included as a component part of the State of Montana Basic Financial Statements, which are prepared annually and presented in the Montana Comprehensive Annual Financial Report (CAFR).

The University, as a political subdivision of the State of Montana, is excluded from Federal income taxes under Section 115(1) of the Internal Revenue Code, as amended. Certain activities of the University may be subject to taxation as unrelated business income under Internal Revenue Code Sections 511 to 514.

▪ BASIS OF PRESENTATION

The financial statements have been prepared in accordance with generally accepted accounting principles, as prescribed by the Governmental Accounting Standards Board (GASB). Under GASB Statement No. 34, “Basic Financial Statements and Management Discussion and Analysis for State and Local Governments” and GASB Statement No. 35, “Basic Financial Statements and Management’s Discussion and Analysis for Public Colleges and Universities,” the University is required to present a Statement of Net Assets, a Statement of Revenues, Expenses

and Changes in Net Assets, and a Statement of Cash Flows. All significant intra-entity transactions have been eliminated upon consolidation.

Also, in accordance with GASB Statement No. 39, the combined statement of financial position and statement of activities of the four component units referred to above are separately presented following the respective University financial statements.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

▪ BASIS OF ACCOUNTING

For financial reporting purposes, the University is considered a special-purpose government engaged only in business-type activities. Business-type activities are those that are financed in whole or in part by fees charged to external parties for goods or services. Accordingly, the University's consolidated financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when an obligation has been incurred.

The University had the option to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless FASB conflicts with GASB. The University elected to not apply FASB pronouncements issued after the applicable date.

▪ USE OF ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from these estimates.

▪ CASH EQUIVALENTS

For purposes of the Consolidated Statement of Cash Flows, the University considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. Funds invested in Guaranteed Investment Contracts (GICs) and in the Short Term Investment Pool (STIP) with the Montana Board of Investments are considered cash equivalents.

▪ INVESTMENTS

The University accounts for its investments at fair value in accordance with GASB Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools." Investment income is recorded on the accrual basis. All investment income, including changes in unrealized gain (loss) on the carrying value of investments, is reported as a component of investment income.

▪ ACCOUNTS AND GRANTS RECEIVABLE

Accounts receivable consists of tuition and fee charges to students and to auxiliary enterprise services provided to students, faculty and staff. Accounts receivable also includes amounts due from the federal government and local governments, or private sources, in connection with reimbursement of allowable expenditures made pursuant to the University's grants and contracts. Accounts receivable is recorded net of estimated uncollectible amounts.

▪ INVENTORIES

Inventories are comprised of consumable supplies, food items and items held for resale or recharge within the University. The larger inventories are valued using the moving-average method. Other inventories are valued using First In First Out (FIFO) or specific identification methods.

▪ CASH AND SHORT-TERM INVESTMENTS

Cash and investments that are externally restricted to make debt service payments, or by a donor or outside agency prohibiting the expenditure of principal and possibly earnings, are classified as non-current assets in the Consolidated Statement of Net Assets.

Notes to the Consolidated Financial Statements (continued)

▪ CAPITAL ASSETS

Capital assets are stated at cost or fair market value at date of purchase or donation. Renovations to buildings, infrastructure, and land improvements that significantly increase the value or extend the useful life of the asset are capitalized. Routine repairs and maintenance are charged to operating expense in the year in which the expense was incurred. Buildings, building improvements and land improvements, and infrastructure are capitalized when acquisition costs equal or exceed \$25,000 and \$500,000, respectively. Equipment is capitalized when acquisition costs equal or exceed \$5,000.

Depreciation is computed on a straight-line basis over the estimated useful lives of the respective assets as follows: buildings - 40 years; land improvements and infrastructure - 20 and 40 years, respectively; library books - 8 years; and equipment- 3 to 10 years. Historically, the University has capitalized all artwork subject to applicable capitalization policies at the time of donation or purchase. The University has elected to continue to capitalize artwork subject to the current threshold, but without recording depreciation on those items.

▪ DEFERRED REVENUE

Deferred revenues include amounts received for tuition and fees and certain auxiliary activities prior to the end of the fiscal year but related to the subsequent accounting period. Deferred revenues also include amounts received from grant and contract sponsors that have not yet been earned.

▪ COMPENSATED LEAVE

Eligible University employees earn eight hours sick leave and ten hours annual leave for each month worked. The accrual rate for annual leave increases with length of service. The maximum annual leave that eligible employees may accumulate is two hundred percent of their annual accrual. Sick leave may accumulate without limitation. Twenty-five percent of accumulated sick leave earned after July 1, 1971, and one hundred percent of accumulated annual leave, if not used during employment, is paid upon termination.

▪ NET ASSETS

The University's net assets are categorized as follows:

- **Invested in capital assets, net of related debt** - Capital assets, net of accumulated depreciation and outstanding principal balances of debt attributable to the acquisition, construction or improvement of those assets.
- **Restricted, nonexpendable** - Net assets subject to externally imposed stipulations that the University maintain those assets permanently. Such assets include the University's permanent endowment funds.
- **Restricted, expendable** - Net assets whose use by the University is subject to externally imposed stipulations that can be fulfilled by actions of the University pursuant to those stipulations or that expire by the passage of time.
- **Unrestricted** - Net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Regents, or may otherwise be limited by contractual agreements with outside parties. Substantially all unrestricted net assets are designated for academic and research programs and initiatives, and capital programs.

▪ CLASSIFICATION OF REVENUES

The University has classified its revenues as either operating or non-operating revenues according to the following criteria:

- **Operating revenue** - Operating revenues include activities that have the characteristics of exchange transactions, such as (1) student tuition and fees, net of scholarship discounts and allowances, (2) sales and services of auxiliary enterprises, net of scholarship discounts and allowances, (3) most federal, state and local grants and contracts and federal appropriations, and (4) interest on institutional student loans.
- **Non-operating revenues** - Non-operating revenues include activities that have the characteristics of non-exchange transactions, such as gifts and contributions, and other revenue sources that are defined as non-operating revenues by GASB No. 9, "Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting," and GASB No. 34,

“Basic Financial Statements and Management Discussion and Analysis for State and Local Governments.” Types of revenue sources that fall into this classification are state appropriations and investment income.

▪ **USE OF RESTRICTED REVENUES**

When the University maintains both restricted and unrestricted funds for the same purpose, the order of use of such funds is determined on a case-by-case basis. Restricted funds remain classified as restricted until they have been expended.

▪ **SCHOLARSHIP DISCOUNTS AND ALLOWANCES**

Student tuition and fee revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances in the Statements of Revenues, Expenses, and Changes in Net Assets. Scholarship discounts and allowances are generated by the difference between the stated charge for goods and services provided by the University, and the amount that is paid by students and/or third parties making payments on the students' behalf. Certain governmental grants, such as Pell grants, and other federal, state or nongovernmental programs, are recorded as either operating or non-operating revenues in the University's consolidated financial statements. To the extent that revenues from such programs are used to satisfy tuition and fees and other student charges, the University has recorded a scholarship discount and allowance.

• **RECLASSIFICATION AND RESTATEMENT**

In order to make certain prior year amounts comparable to the current year presentation on the Consolidated Statement of Revenues, Expenses and Changes in Net Assets, graduation teaching assistant fee waivers of \$3,726,071 were reclassified to compensation and employee benefits from scholarships and fellowships. The change in classification of these expenditures also required a reduction of \$3,126,232 to the tuition discounting amount previously reported. The cash flows from operating activities in the Consolidated Statement of Cash Flows for the prior year was adjusted accordingly to reflect the reclassification and restatement described above.

NOTE 3 – CASH EQUIVALENTS AND INVESTMENTS

▪ **CASH EQUIVALENTS**

Cash equivalents consist of cash invested in Guaranteed Investment Contracts (GICs) with Transamerica Occidental, and in the STIP with the Montana Board of Investments. Amounts held in cash equivalents at June 30, 2007 and 2006 were \$57,006,960 and \$55,095,471 respectively. At June 30, 2007, \$17,111,852 of unexpended proceeds from the issuance of Facility Improvement Revenue Bonds, were invested in GIC accounts and is included in the total cash equivalents of \$57,006,690. STIP investments are purchased in accordance with the statutorily mandated "Prudent Expert Principle." The STIP portfolio may include asset-backed securities, commercial paper, corporate and government securities, repurchase agreements and variable rate, or floating rate, instruments to provide diversification and a competitive rate of return. Investments in STIP and GICs may be withdrawn by the University on demand, and as such, are classified as cash equivalents.

▪ **INVESTMENTS**

Investments consisted of the following at June 30, 2007 and 2006:

Security Type	Fair Value		Effective Duration at June 30, 2007*	Credit Quality Rating at June 30, 2007***
	2007	2006		
U.S. Government Indirect – Backed	\$ 2,056,148	\$ 3,350,033	1.697	N/A
U.S. Government Direct – Backed	-	219,292	-	-
Trust Fund Bond Pool (TFBP)	5,727,734	5,507,471	5.25**	NR
Montana Domestic Equity Pool (MDEP)	1,318,308	1,110,293	Not Applicable	N/A
Foundation Pooled Investments	17,802,727	14,626,407	Not Applicable	N/A
Certificates of Deposits	270,530	258,342	.939	N/A
Total investments	\$ 27,175,447	\$ 25,266,838		
Securities Lending Collateral Investment Pool	\$ 317,923	\$ 836,492		

Notes to the Consolidated Financial Statements (continued)

*See Interest Rate Risk under the Investment Risks disclosure included in this note.

**Effective duration for the Trust Fund Bond Pool (TFBP) is for the entire portfolio. The University's ownership represents less than 0.5% of the portfolio

***NR indicates security investment unrated for credit quality type.

Investments held by the University at June 30, 2007 and 2006 are described further in the paragraphs below.

U.S. Government Securities

U.S. Government securities consist of bond trustee funds managed by U.S. Bank. The U.S. Government securities portfolio includes Treasury securities or other Federal agency securities, and federal money market accounts. All of the securities were registered under the nominee's name (U.S. Bank) on behalf of the University.

Montana Board of Investments Pools

The University is a participant in certain internal investment pools administered by the Montana Board of Investments (MBOI). MBOI purchases investments for each portfolio in accordance with the statutorily mandated "Prudent Expert Principle." The University was invested in the following internal investment pools at June 30, 2007 and 2006:

Montana Domestic Equity Pool (MDEP)

The MDEP portfolio may include common stock, equity index, preferred stock, convertible equity securities, American Depositary Receipts (ADR's) and equity derivatives. ADR's are receipts issued by a U.S. depositary bank representing shares of a foreign stock or bonds held abroad by the foreign sub-custodian of the American depositary bank. Equity derivatives "derive" their value from other equity instruments such as futures and options.

Trust Funds Bond Pool (TFBP)

The TFBP portfolio includes corporate asset-backed, other corporate, U.S. government mortgage-backed, and Yankee securities. The TFBP portfolio includes securities classified as corporate, foreign government bonds, municipals, U.S. government direct-backed, U.S. government indirect-backed, and cash equivalents. U.S. government direct-backed securities include direct obligations of the U.S. Treasury and obligations explicitly guaranteed by the U.S. government. U.S. government indirect-backed obligations include U.S. government agency and mortgage-backed securities. U.S. government mortgage-backed securities reflect participation in a pool of residential mortgages.

The TFBP portfolio includes structured financial instruments known as REMICs (Real Estate Mortgage Investment Conduits). REMICs are pass-through vehicles for multiclass mortgage-backed securities.

The University Foundation Pools

This pool consists of endowment funds held in a common investment pool administered by the University of Montana and Montana Tech Foundations.

Certificates of deposit

Certificates of deposit serve as collateral for loans made to students with disabilities for the purchase of specialized equipment necessary to complete their education. The certificate of deposit, including interest earned, is reinvested upon maturity.

Securities lending transactions

Under the provisions of state statutes, the Board of Investments, via a Securities Lending Authorization Agreement, has authorized the custodial bank, State Street Bank and Trust, to lend the Board of Investment's securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. During the period the securities are on loan, the Board of Investments receives a fee and the custodial bank must initially receive collateral equal to 102 percent of the market value of the loaned securities and maintain collateral equal to not less than 100 percent of the market value of the loaned security. The Board of Investments retains all rights and risks of ownership during the loan period.

During the years ending June 30, 2007 and 2006, the Board of Investments and the borrowers maintained the right to terminate all securities lending transactions on demand. The cash collateral received on each loan was invested, together with the cash collateral of other qualified-plan lenders, in a collective investment pool, the Securities Lending Quality Trust. The relationship between the average maturities of the investment pool and the Board of Investment's loans was affected by the maturities of the loans made by other plan entities that invested cash collateral in the collective investment pool, which the Board of Investments could not determine. At June 30, 2007 and 2006, the Board of Investments had no credit risk exposure to borrowers.

Investment risks

Effective June 30, 2005, the University implemented the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40, "Deposit and Investment Risk Disclosures."

Investment risks associated with the University's investments are described in the following paragraphs:

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. In accordance with GASB Statement No. 40, the State of Montana has selected the effective duration method to disclose interest rate risk. Duration is a measure of a debt's exposure to fair value changes from changing interest rates. It uses the present value of the cash flows from the investment, weighting those cash flows as a percentage of the investment's full price. The University does not have a formal investment policy for interest rate risk.

Credit Risk

Credit risk is defined as the risk that an issuer or other counterparty to an investment will not fulfill its obligation. The University does not have a formal investment policy for credit risk. With the exception of the U.S. government securities, all STIP securities and TFBP fixed income instruments have credit risk as measured by major credit rating services.

U.S. government securities are guaranteed directly or indirectly by the U.S. government. Obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk and do not require disclosure of credit quality.

Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of the investment or collateral securities that are in the possession of an outside party. The University does not have a formal investment policy for custodial credit risk. As of June 30, 2007 and 2006, all STIP, MDEP and TFBP securities were registered in the nominee name for the MBOI and held in the possession of the Board's custodial bank, State Street Bank.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributed to the magnitude of a government's investment in a single issuer. The University does not have a formal policy for concentration of credit risk. Investments issued or explicitly guaranteed by the U.S. government are excluded from the concentration of credit risk requirement. MDEP investments in pooled investments, such as the BGI Equity Index and DFA Small Cap Subtrust investments, are also excluded from this requirement.

Notes to the Consolidated Financial Statements (continued)

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Land grant earnings

In 1881, the Congress of the United States granted land to the State of Montana for the benefit of the state's universities and colleges. The Enabling Act of 1889 granted 46,563 acres to Missoula, 100,000 acres to Montana Tech and 50,000 acres to Western Montana College. Under provisions of the grants, proceeds from the sale of land and land assets, together with proceeds from the sale of timber, oil royalties and other minerals, must be reinvested, and constitute, along with the balance of unsold land, a perpetual trust fund. The grant is administered as a trust by the State Land Board, which holds title and has the authority to direct, control, lease, exchange and sell these lands. The University, as a beneficiary, does not have title to the assets resulting from the grant, only a right to the earnings generated. The University's share of the trust earnings was \$1,505,512 and \$1,452,867 for the years ended June 30, 2007 and 2006, respectively. These earnings are currently pledged to the Series C 1995, Series E 1998, Series F 1999, Series G 2002, Series H 2003, Series I 2004, and Series J 2005 revenue bonds.

The University's land grant assets are not reflected in the consolidated financial statements, but are included as a component of the State of Montana Basic Financial Statements that are prepared annually and presented in the Montana Comprehensive Annual Financial Report (CAFR).

NOTE 4 – ACCOUNTS AND GRANTS RECEIVABLE

Accounts Receivable consisted of the following at June 30, 2007 and 2006:

	2007	2006
Student tuition and fees	\$ 1,460,483	\$ 1,545,029
Auxiliary enterprises and other operating activities	1,200,425	1,355,001
Private grants and contracts	2,523,859	1,392,136
Other	821,252	440,384
	6,006,019	4,732,550
Less: allowance for doubtful accounts	333,723	208,356
	\$ 5,672,296	\$ 4,452,194

NOTE 5 – LOANS RECEIVABLE

Student loans made under the Federal Perkins Loan Program constitute the majority of the University's loan receivable balances. Included in non-current liabilities as of June 30, 2007 and 2006 are \$10,020,616 and 9,875,660, respectively, that would be refundable to the Federal Government should the University choose to cease participation in the Federal Perkins Loan program.

The Federal portion of interest income and loan program expenses is shown as additions to and deductions from the amount due to the Federal government, and not as operating transactions, in the Consolidated Statement of Net Assets.

NOTE 6 – INVENTORIES

Inventories consisted of the following at June 30, 2007 and 2006:

	2007	2006
Bookstore	\$ 709,927	\$ 595,787
Food services	117,814	120,306
Facilities services	697,431	718,470
Other	277,251	325,417
	\$ 1,802,423	\$ 1,759,980

NOTE 7 – CAPITAL ASSETS

The following tables present the changes in capital assets for the years ended June 30, 2007 and 2006, respectively.

For the year ended June 30, 2007:

	Beginning Balance	Additions	Deletions	Transfers and Other Changes	Ending Balance
Capital assets not being depreciated:					
Land	\$ 7,125,781	\$ -	\$ -	\$ -	\$ 7,125,781
Capitalized Collections	15,461,417	779,533	30,500	-	16,210,450
Construction in progress	29,691,709	24,867,970	-	(2,530,743)	52,028,936
	52,278,907	25,647,503	30,500	(2,530,743)	75,365,167
Other capital assets:					
Buildings	203,800,450	342,316	-	-	204,142,766
Building improvements	127,504,476	-	-	2,468,479	129,972,955
Furniture and equipment	46,344,468	4,609,591	959,950	(53,161)	49,940,948
Land improvements	12,619,381	-	-	-	12,619,381
Livestock	34,197	-	10,000	-	24,197
Library materials	49,289,112	1,633,880	-	(2,560)	50,920,432
	439,592,084	6,585,787	969,950	2,412,758	447,620,679
Less accumulated depreciation for:					
Buildings	91,680,684	4,497,624	-	-	96,178,308
Building improvements	72,214,239	6,692,850	-	-	78,907,089
Furniture and equipment	29,233,638	3,491,646	892,168	120	31,833,236
Livestock	7,685	3,165	2,417	-	8,433
Land improvements	8,220,918	350,050	-	-	8,570,968
Library materials	42,744,327	1,560,137	-	76,445	44,380,909
	244,101,491	16,595,472	894,585	76,565	259,878,943
Other capital assets, net	195,490,593	(10,009,685)	75,365	2,336,193	187,741,736
Intangible assets	502,879	82,000	205	(246,893)	337,781
Total capital assets, net	\$ 248,272,379	\$ 15,719,818	\$ 106,070	\$ (441,443)	\$ 263,444,684
Capital Asset Summary:					
Capital assets not being depreciated	\$ 52,278,907	\$ 25,647,503	\$ 30,500	\$ (2,530,743)	\$ 75,365,167
Other capital and intangible assets	440,094,963	6,667,787	970,155	2,165,865	447,958,460
	492,373,870	32,315,290	1,000,655	(364,878)	523,323,627
Less: accumulated depreciation	244,101,491	16,595,472	894,585	76,565	259,878,943
Total capital assets, net	\$ 248,272,379	\$ 15,719,818	\$ 106,070	\$ (441,443)	\$ 263,444,684

For the year ended June 30, 2006:

	Beginning Balance	Additions	Deletions	Transfers and Other Changes	Ending Balance
Capital assets not being depreciated:					
Land	\$ 7,125,781	\$ -	\$ -	\$ -	\$ 7,125,781
Capitalized Collections	15,270,723	190,694	-	-	15,461,417
Construction in progress	13,365,371	18,224,036	-	(1,897,698)	29,691,709
	35,761,875	18,414,730	-	(1,897,698)	52,278,907

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Other capital assets:

Buildings	203,800,450	-	-	-	203,800,450
Building improvements	126,111,619	-	-	1,392,857	127,504,476
Furniture and equipment	47,834,423	6,084,894	7,485,658	(89,191)	46,344,468
Land improvements	12,220,369	-	-	399,012	12,619,381
Livestock	34,197	-	-	-	34,197
Library materials	47,996,834	1,404,226	111,948	-	49,289,112
	437,997,892	7,489,120	7,597,606	1,702,678	439,592,084

Less accumulated depreciation for:

Buildings	87,113,683	4,567,001	-	-	91,680,684
Building improvements	65,614,368	6,599,871	-	-	72,214,239
Furniture and equipment	32,930,955	3,229,243	6,926,560	-	29,233,638
Livestock	3,603	4,082	-	-	7,685
Land improvements	7,879,127	341,791	-	-	8,220,918
Library materials	41,198,807	1,657,467	111,947	-	42,744,327
	234,740,543	16,399,455	7,038,507	-	244,101,491

Other capital assets, net

203,257,349	(8,910,335)	559,099	1,702,678	195,490,593
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Intangible assets

724,504	89,302	-	(310,927)	502,879
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Total capital assets, net

\$ 239,743,728	\$ 9,593,697	\$ 559,099	\$ (505,947)	\$ 248,272,379
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Capital Asset Summary:

Capital assets not being depreciated	\$ 35,761,875	\$ 18,414,730	\$ -	\$ (1,897,698)	\$ 52,278,907
Other capital and intangible assets	438,722,396	7,578,422	7,597,606	1,391,751	440,094,963
	474,484,271	25,993,152	7,597,606	(505,947)	492,373,870
Less: accumulated depreciation	234,740,543	16,399,455	7,038,507	-	244,101,491
Total capital assets, net	\$ 239,743,728	\$ 9,593,697	\$ 559,099	\$ (505,947)	\$ 248,272,379

NOTE 8 – LONG – TERM LIABILITIES

The following tables present the changes in long-term liabilities for the years ended June 30, 2007 and 2006, respectively:

For the year ended June 30, 2007:

	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Bonds, notes and capital leases					
Revenue bonds payable, net	\$ 150,007,775	\$ 268,303	\$ 5,154,681	\$145,121,397	\$ 5,610,000
Notes payable	1,590,964	-	660,473	930,491	418,470
Capital leases payable	636,037	32,866	237,766	431,137	151,404
	152,234,776	301,169	6,052,920	146,483,025	6,179,874
Other long-term liabilities					
Accrued compensated absences	19,359,552	9,118,942	8,088,384	20,390,110	8,290,619
Advances from primary government	5,841,295	-	374,818	5,466,477	390,118
Due to Federal Government	9,875,660	144,956	-	10,020,616	-
Derivative financial instrument	2,094,500	-	-	2,094,500	-
	37,171,007	9,263,898	8,463,202	37,971,703	8,680,737
Total long-term liabilities	\$ 189,405,783	\$ 9,565,067	\$ 14,516,122	\$ 184,454,728	\$ 14,860,611

For the year ended June 30, 2006:

	Beginning Balance	Additions	Deductions	Ending Balance	Current Portion
Bonds, notes and capital leases					
Revenue bonds payable, net	\$ 134,785,340	\$ 31,430,847	\$ 16,208,412	\$ 150,007,775	\$ 5,105,000
Notes payable	2,020,728	-	429,764	1,590,964	387,096
Capital leases payable	498,489	444,297	306,749	636,037	233,246
	137,304,557	31,875,144	16,944,925	152,234,776	5,725,342
Other long-term liabilities					
Accrued compensated absences	18,236,084	8,525,259	7,401,791	19,359,552	7,763,180
Advances from primary government	5,890,671	484,835	534,211	5,841,295	374,816
Due to Federal Government	9,696,369	179,291	-	9,875,660	-
Derivative financial instrument	-	2,094,500	-	2,094,500	-
	33,823,124	11,283,885	7,936,002	37,171,007	8,137,995
Total long-term liabilities	\$ 171,127,681	\$ 43,159,029	\$ 24,880,927	\$ 189,405,783	\$ 13,863,338

▪ LONG-TERM LIABILITIES

Long-term liabilities include:

- capital lease obligations, principal amounts of bonds payable, revenue bonds payable, and notes payable with contractual maturities greater than one year;
- estimated amounts for accrued compensated absences and other liabilities that will not be paid within the next fiscal year; and
- other liabilities that, although payable within one year, are to be paid from funds that are classified as non-current assets.

Interest Rate Exchange Agreement

In August, 2005 the University entered into a forward SWAP agreement (“swaption”) with Wachovia Bank, NA (“counterparty”) to hedge the interest rate risk associated with the potential future issuance of variable-rate revenue bonds. In exchange, the University received \$2,094,500 from the counterparty. A portion of the payment was consideration for the estimated present value of the fixed rate payable under the agreement upon execution of the swaption. The swaption gives the counterparty the right to require that the University execute a floating to fixed swap in May 2010, based on a notional amount of \$47,000,000. Should the counterparty exercise its option, the University would expect to issue Series K 2010 taxable, variable rate bonds at the \$47,000,000 notional amount of the swap. The intention of the University in entering into the swaption is to refund its outstanding Series F 1999 Revenue Bonds and lower the cost of its borrowing.

Terms – The counterparty has the right to exercise the swap on May 15, 2010, the call date of the Series F 1999 Revenue Bonds. If the swaption is exercised it will also become effective on May 15, 2010. Under terms of the swap, the University will pay the counterparty a fixed rate substantially equal to the fixed rate on the refunded bonds and receive a variable payment based on the one-month LIBOR rate, plus 30 basis points.

Once the refunded Series F 1999 Revenue Bonds escrow matures in 2019, the floating rate Series K 2010 Parity Bonds will be converted to tax-exempt bonds and the swap will convert to tax exempt rates as well. Should the option to enter the swap not be exercised by the counterparty, the University would not be required to repay the swaption purchase price.

Fair Value – At June 29, 2007, the swaption has a negative fair value of \$834,249. Such value was provided to the University by the counterparty, and was calculated as an approximation of market value derived from proprietary models and from certain other financial information believed to be reliable by the counterparty. The negative fair value of the swaption indicates that the fixed rate the University would pay under the potential transaction exceeded the one-month London InterBank Offering Rate (LIBOR) at June 29, 2007.

Notes to the Consolidated Financial Statements (continued)

Market-access risk – If the option is exercised and variable-rate Series K 2010 Parity Bonds are not issued by the University, the Series F 1999 Revenue Bonds would not be refunded, and the University would make net swap payments as required by the terms of the swap.

Capital Leases

The University has future minimum lease commitments for capital lease obligations consisting of the following at June 30, 2007:

<u>Fiscal Year</u>	<u>Total</u>
2008	\$ 185,980
2009	163,319
2010	114,849
2011	30,868
Minimum lease payments	\$ 495,016
Less: Amount representing interest	63,879
Present value of net minimum lease payments	<u>\$ 431,137</u>

NOTE 9 – REVENUE BONDS

Revenue bonds were issued pursuant to an Indenture of Trust between the Board of Regents of Higher Education for the State of Montana (on behalf of The University of Montana) and U. S. Bank Trust National Association MT. The bonds are secured by a first lien on the combined pledged revenues of the four campuses of The University of Montana. The pledged revenues earned at each campus are cross-pledged among all campuses of The University of Montana. Bonds payable recorded by each campus reflect the liability associated with the bond proceeds deposited into the accounts of that campus and do not necessarily mean that the debt service payments on that liability will be made by that campus.

The total aggregate principal amount originally issued pursuant to the Indenture of Trust and the various supplements to the Indenture for all campuses of The University of Montana at June 30, 2007 and 2006, was \$169,426,780. The combined principal amount outstanding at June 30, 2007 and 2006 was \$147,564,997 and \$152,669,997, respectively.

Series C 1995

On December 14, 1995, The University of Montana issued \$34,406,784 of Series C 1995 Revenue Bonds, with interest ranging from 3.80 percent to 5.75 percent. In fiscal year 2000, the Series F 1999 Revenue Bonds issuance advance refunded a portion of Series C 1995 revenue bonds.

Series E 1998

On June 26, 1998, The University of Montana issued \$10,670,000 of Series E 1998 Revenue Bonds, with interest ranging from 3.90 percent to 5.00 percent. The proceeds from the issue provided funds for the acquisition, construction, repair, replacement, renovation and improvement of certain facilities and properties.

Series F 1999

On November 12, 1999, The University of Montana issued \$69,240,000 of Series F 1999 Revenue Bonds, with interest rates ranging from 3.80 percent to 6.00 percent. The proceeds from the issue were used for the purpose of restructuring Series B, C and D Facilities Improvement Revenue Bonds, and for the acquisition, construction, remodeling, improvement and equipping certain facilities and properties at The University of Montana.

The University of Montana recorded \$58,205,000 of the Series F 1999 Revenue Bonds to advance refund \$58,609,189 of outstanding Series B, C and D Facilities Improvements Revenue Bonds with average interest rates ranging from 4.30 percent to 6.65 percent. The Series B, C and D Facilities Improvements Revenue Bonds are considered legally defeased and as a result, the liability for those bonds is no longer recorded in the consolidated financial statements.

Included in the Series F issuance was \$10,650,000 for construction of a new recreation facility at University's Missoula campus. In September, 2005, the Series J 2005 Revenue Bond issuance advanced refunded the outstanding principal amount of this portion of the Series F 1999 issuance (see Series J 2005 below).

Series G 2002

On October 18, 2002, The University of Montana issued \$18,900,000 of Series G Facilities Improvement Revenue Bonds, with interest ranging from 3.00 percent to 4.65 percent. The proceeds from the issue provided funds for the acquisition, construction, furnishing and equipping of certain student housing facilities on the Missoula campus.

Series H 2003

In April 2003, The University of Montana issued \$1,015,000 of Series H Facilities Improvement Revenue Bonds, with interest at 2.70 percent. The proceeds from the issue provided funds for the Washington Grizzly Stadium expansion on the Missoula campus.

Series I 2004

In April 2004, The University of Montana issued \$40,490,000 of Series I Refunding and Facilities Improvement Revenue Bonds, with interest ranging from 3.00 percent to 4.75 percent. The proceeds from the issue paid and discharged \$30,540,000 of Series A 1993, Revenue Bonds. The issuance also provided \$7,000,000 towards future expansion of the Skaggs Building and \$2,950,000 for deferred maintenance on the Missoula campus.

Series J 2005

On September 15, 2005, The University of Montana issued \$31,095,000 of Series J 2005 Facilities Improvement and Refunding Revenue Bonds, with interest ranging from 3.0 percent to 4.5 percent. The proceeds from the issue, together with certain resources of the University, will provide funds to pay and discharge a portion of the Series F Revenue Bonds, and finance or refinance, the costs of acquisition, construction, furnishing, equipping, renovation or improvement of certain University facilities.

The University of Montana recorded \$11,120,000 of the Series J 2005 Revenue Bonds to advance refund \$10,010,000 of outstanding Series F Facilities Improvement Revenue Bonds to reduce annual debt service payments. The interest rates on the advanced refunded revenue bonds ranged from 4.80 percent to 6.00 percent. The Series F Facilities Improvement Revenue Bonds are considered legally defeased and as a result, the liability for those bonds is no longer recorded in the consolidated financial statements. The debt service cash flows for Series J 2005 Revenue Bonds (Refunding portion) are less than the debt service cash flows for the advanced refunded bonds by \$862,000. The economic gain for The University of Montana from the advanced refunding was \$600,786 (difference between the present values of the debt service payments on the old and new debt).

Defeased Bonds

The University has defeased certain bond issues by placing proceeds of new bonds in an irrevocable trust. The proceeds, together with interest earned thereon, will be sufficient for future debt service payments on the refunded issues. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the University's consolidated financial statements. As of June 30, 2007 and 2006, \$ 51,481,125 and \$54,277,074, respectively, of bonds outstanding were considered defeased.

Notes to the Consolidated Financial Statements (continued)

Revenue Bonds Payable

As of June 30, 2007 annual principal payments are as follows:

Series C 1995 (Partial)		
Fiscal Year	Interest Rate	Principal
2008	5.00%	\$ 450,000
2009	5.10%	475,000
2010	5.20%	495,000
2011	5.25%	525,000
		<u>\$ 1,945,000</u>

Series E 1998		
Fiscal Year	Interest Rate	Principal
2008	4.45%	\$ 375,000
2009	4.50%	405,000
2010	4.60%	310,000
2011	4.70%	460,000
2012	4.80%	470,000
2013-2017	5.00%	2,305,000
2018-2021	5.00%	2,525,000
		<u>6,850,000</u>
Less unamortized discount:		22,278
		<u>\$ 6,827,722</u>

Series F 1999		
Fiscal Year	Interest Rate	Principal
2008	5.00%	\$ 245,000
2009	5.10%	285,000
2010	5.20%	460,000
2011	5.35%	345,000
2012	5.25%	915,000
2013-2017	5.375 - 5.75%	10,964,997
2018-2022	5.75 - 6.00%	29,020,000
2023-2024	5.75%	15,290,000
		<u>57,524,997</u>
Less unamortized discount:		833,704
		<u>\$ 56,691,293</u>

Series G 2002		
Fiscal Year	Interest Rate	Principal
2008	3.00%	\$ 465,000
2009	3.00%	480,000
2010	3.15%	420,000
2011	3.30%	430,000
2012	3.40%	445,000
2013-2017	3.60-4.10%	2,480,000
2018-2022	4.20-4.60%	3,030,000
2023-2027	4.65%	3,795,000
2028-2032	4.65%	4,775,000
2033	4.65%	1,095,000
		<u>17,415,000</u>
Less unamortized discount:		41,700
		<u>\$ 17,373,300</u>

Series H 2003

Fiscal Year	Interest Rate	Principal
2008	2.70%	\$ 215,000
		<u>\$ 215,000</u>

Series I 2004

Fiscal Year	Interest Rate	Principal
2008	3.00%	\$ 2,620,000
2009	3.00-3.50%	2,660,000
2010	3.50%	2,710,000
2011	3.50%	2,800,000
2012	3.50-4.75%	2,905,000
2013-2017	3.70-4.75%	11,430,000
2018-2022	4.375%	455,000
2023-2027	4.375 - 4.50%	7,410,000
2028-2030	4.50%	1,365,000
		<u>34,355,000</u>
Add net unamortized premium:		907,373
		<u>\$ 35,262,373</u>

Series J 2005

Fiscal Year	Interest Rate	Principal
2008	3.50%	\$ 1,240,000
2009	4.00%	1,285,000
2010	4.50%	1,330,000
2011	4.50%	990,000
2012	4.25%	1,045,000
2013-2017	4.00 -4.50%	5,740,000
2018-2022	4.00-4.25%	6,800,000
2023-2027	4.00- 4.25%	7,505,000
2028-2030	4.25%	3,325,000
		<u>29,260,000</u>
Add net unamortized premium:		48,299
		<u>\$ 29,308,299</u>

Revenue Bond Payable Summary:

Total revenue bonds outstanding	147,564,997
Add: Net unamortized premiums and discounts	57,990
Less: Unamortized loss on advance refunding	<u>2,501,590</u>
Revenue bonds payable, net	<u>\$ 145,121,397</u>

The scheduled maturities of the revenue bonds payable are as follows:

Fiscal Year	Principal	Interest	Total Payment
2008	\$ 5,610,000	\$ 7,034,647	\$ 12,644,647
2009	5,590,000	6,858,006	12,448,006
2010	5,725,000	6,644,551	12,369,551
2011	5,550,000	6,411,002	11,961,002
2012	5,780,000	6,199,616	11,979,616
2013-2017	32,919,997	26,807,174	59,727,171
2018-2022	41,830,000	17,783,837	59,613,837
2023-2027	34,000,000	6,174,210	40,174,210
2028-2032	9,465,000	1,352,031	10,817,031
2033	1,095,000	50,918	1,145,918
	<u>\$ 147,564,997</u>	<u>\$ 85,315,992</u>	<u>\$ 232,880,989</u>

NOTE 10 – NOTES PAYABLE

Notes payable at June 30, 2007 consisted of the following:

Description	Interest Rate	Maturity Date	Principal Outstanding	Current Maturities
First Interstate Bank	7.00%	15-Oct-15	\$ 181,882	\$ 17,193
Ames Construction, Inc.	3.085%	01-Nov-08	358,205	358,204
Wells Fargo Bank	4.48%	1-May-15	390,404	43,073
			\$ 930,491	\$ 418,470

The scheduled maturities of the notes payable are as follows:

Fiscal Year	Principal	Interest	Total Payment
2008	\$ 418,470	\$ 40,301	\$ 458,771
2009	61,928	29,476	91,404
2010	65,233	22,786	88,019
2011	68,722	19,297	88,019
2012	72,391	15,628	88,019
2013-2016	243,747	22,604	266,351
	\$ 930,491	\$ 150,092	\$ 1,080,583

NOTE 11 – COMPENSATED LEAVE

Employee compensated absences are accrued at year-end for consolidated financial statement purposes. The liability and expense incurred are recorded at year-end as accrued compensated absences in the Statements of Net Assets, and as a component of compensation and benefit expense in the Statements of Revenues, Expenses, and Changes in Net Assets.

NOTE 12 – ADVANCES FROM PRIMARY GOVERNMENT

Advances from the primary government are received through the InterCap Program offered through the Montana Board of Investments. The program lends money to state agencies, including the Montana University System, for the purpose of financing or refinancing the acquisition and installation of equipment or personal and real property and infrastructure improvements.

The Montana Science and Technology Alliance (MSTA) loan originates from a loan that was originally issued in 1994, and has a remaining term of 55 years. The interest rates are variable and are adjusted annually.

Advances from Primary Government at June 30, 2007, are as follows:

Description	Interest Rate	Maturity Date	Principal Outstanding
InterCap – Weight Room Expansion	Variable	15-Feb-09	\$ 56,197
InterCap – Lubrecht Forest	Variable	15-Aug-08	32,415
InterCap – IT Wiring and Fiber	Variable	15-Aug-10	164,750
InterCap – Real Estate	Variable	15-Feb-12	49,135
InterCap – Intercollegiate Athletics	Variable	15-Feb-10	166,788
InterCap – Public Safety	Variable	15-Aug-16	277,334
InterCap – Dining Services	Variable	15-Aug-08	7,753
InterCap – Forestry	Variable	15-Aug-14	774,002
InterCap – Campus Mail	Variable	15-Aug-08	5,093
InterCap – Facility Services	Variable	15-Feb-10	53,232

Intercap – Public Safety	Variable	15-Feb-13	312,450
Intercap – Microwave Network	Variable	15-Aug-11	46,381
MSTA loan – Research Offices	Variable	30-June-61	3,520,947
			<u>5,466,477</u>
Less Current Maturities			390,118
			<u>\$ 5,076,359</u>

The scheduled maturities of the Intercap loans and MSTa loan are as follows:

Fiscal Year	Principal	Interest	Total Payment
2008	\$ 390,118	\$ 174,907	\$ 565,025
2009	388,144	157,907	546,051
2010	354,343	141,013	495,356
2011	264,967	125,670	390,637
2012	239,416	114,456	353,872
2013-2017	667,770	449,008	1,116,778
2018-2022	215,704	384,296	600,000
2023-2027	244,018	355,982	600,000
2028-2032	276,049	323,951	600,000
2033-2037	312,285	287,715	600,000
2038-2042	353,277	246,723	600,000
2043-2047	399,650	200,350	600,000
2048-2052	452,109	147,891	600,000
2053-2057	511,455	88,545	600,000
2058-2061	397,172	22,828	420,000
	<u>\$ 5,466,477</u>	<u>\$ 3,221,242</u>	<u>\$ 8,687,719</u>

NOTE 13 – RETIREMENT PLANS

Full-time employees of the University are members of the Public Employees' Retirement System (PERS), Game Wardens' & Peace Officers' Retirement System (GWPORS), Teachers' Retirement System (TRS) or the Optional Retirement Program (ORP) as described below. Only faculty and administrators with contracts under the authority of the Board of Regents are enrolled under TRS or ORP. Beginning July 1, 1993, state legislation required all new faculty and administrators with contracts under the authority of the Board of Regents to enroll in ORP.

PERS, GWPORS and TRS

PERS, GWPORS and TRS are statewide, cost-sharing, multiple-employer defined benefit retirement plans. The plans are established under state law and are administered by the State of Montana. The plans provide retirement, disability, and death benefits to plan members and beneficiaries. PERS, a mandatory system established by the state in 1945, provides retirement services to substantially all public employees. GWPORS, established in 1963, provides retirement benefits for all persons employed as a game warden, warden supervisory personnel, and state police officers not eligible to join the Sheriffs' Retirement System, Highway Patrol Officers' Retirement System, and Municipal Police Officers' Retirement System. TRS, established in 1937, provides retirement services to all persons employed as teachers or professional staff of any public elementary or secondary school, or unit of the University System.

Notes to the Consolidated Financial Statements (continued)

Contribution rates for the plans are required and determined by state law. The contribution rates for 2007 and 2006 expressed as a percentage of covered payrolls were as follows:

	2007			2006		
	Covered Payroll	Employee	Employer	Covered Payroll	Employee	Employer
PERS	\$ 39,256,146	6.90%	6.90%	\$ 36,729,189	6.90%	6.90%
GWPORS	\$ 517,627	10.76%	9.00%	\$ 488,344	10.43%	9.00%
TRS	\$ 20,788,325	9.63%	7.47%	\$ 20,748,781	8.59%	7.47%

The amounts contributed to the plan during years ending June 30, 2007, 2006, and 2005, were equal to the required contribution each year. The amounts contributed were as follows:

	Year ending June 30,		
	2007	2006	2005
<u>PERS</u>			
Employer	\$ 2,710,410	\$ 2,534,423	\$ 2,370,217
Employee	\$ 2,710,756	\$ 2,532,872	\$ 2,370,043
<u>GWPORS</u>			
Employer	\$ 46,586	\$ 43,951	\$ 40,373
Employee	\$ 55,674	\$ 50,944	\$ 44,779
<u>TRS</u>			
Employer	\$ 1,553,068	\$ 1,548,934	\$ 1,685,188
Employee	\$ 2,001,911	\$ 1,782,528	\$ 2,201,136

The plans issue publicly available annual reports that include financial statements and required supplemental information. The reports may be obtained from the following:

Public Employees' Retirement Administration
P.O. Box 200131
100 North Park, Suite 220
Helena, Montana 59620-0131
Phone: (406) 444-3154

Teachers' Retirement Division
P.O. Box 200139
1500 Sixth Avenue
Helena, MT 59620-0139
Phone: (406) 444-3134

ORP

ORP was established in 1988, and is underwritten by the Teachers' Insurance and Annuity Association - College Retirement Equities Fund (TIAA-CREF). The ORP is a defined-contribution plan. Until July 1, 2003, only faculty and staff with contracts under the authority of the Board of Regents were eligible to participate. The plan was changed, effective July 1, 2003, to allow all staff to participate in the ORP. Contribution rates for the plan are required and determined by state law. The University's contributions were equal to the required contribution. The benefits at retirement depend upon the amount of contributions, amounts of investment gains and losses and the employee's life expectancy at retirement. Under the ORP, each employee enters into an individual contract with TIAA-CREF. The University records employee/employer contributions and remits monies to TIAA-CREF. Individuals vest immediately in the employer portion of retirement contributions.

Contributions to ORP (TIAA-CREF) were as follows:

	Year ending June 30,	
	2007	2006
<u>FACULTY</u>		
Covered Payroll	\$59,715,914	\$55,447,659
Employer Contributions	\$2,960,377	\$2,747,986
Percent of Covered Payroll	4.957%	4.956%
Employee Contributions	\$4,209,633	\$3,900,627
Percent of Covered Payroll	7.049%	7.043%

STAFF

Covered Payroll	\$7,686,214	\$7,272,670
Employer Contributions	\$345,880	\$326,543
Percent of Covered Payroll	4.50%	4.49%
Employee Contributions	\$532,427	\$501,815
Percent of Covered Payroll	6.93%	6.90%

For the years ended June 30, 2007 and 2006, \$2,412,523 and \$2,207,843, respectively, or 4.04 percent, was contributed to TRS from ORP faculty employer contributions to amortize past service unfunded liability in accordance with state law. In addition, \$186,546 and, \$175,271 respectively, or 2.42 % was contributed to PERS from ORP staff employer contributions to amortize past service unfunded liability in accordance with state law.

Annual reports that include financial statements and required supplemental information on the plan are available from:

TIAA-CREF
730 Third Avenue
New York, New York 10017-3206
Phone: 1-800-842-2733

NOTE 14 – RISK MANAGEMENT

Due to the diverse risk exposure of the University and its constituent agencies, the insurance portfolio contains a comprehensive variety of coverage. Montana statutes, 2-9-101 through 305, MCA, and ARM 2-2-298, require participation of all state agencies in the self-insurance plan established by the Montana Department of Administration, Risk Management and Tort Defense Division (RMTDD). The self-insurance program includes coverage for commercial general liability, auto liability, professional liability, and errors and omissions exposures. The RMTDD provides coverage, above self-insured retentions, by purchasing other commercial coverage through the state's broker, Willis of Seattle, for excess liability, property, crime, fidelity, boiler and machinery, fine arts, aircraft-liability and hull coverage. The RMTDD also supplies other commercial insurance coverage for specific risk exposures on an as-needed basis such as the Volunteer Accident and Health, Dismemberment and Accidental Death coverage obtained for all units of the Montana University System. In addition to these basic policies, the University has established guidelines in risk assessment, risk avoidance, risk acceptance and risk transfer.

The Tort Claims Act of the State of Montana in section, 2-9-102, MCA, "provides that Governmental entities are liable for its torts and of those of its employees acting within the course and scope of their employment or duties whether arising out of a governmental or proprietary function, except as specifically provided by the Legislature". Accordingly section, 2-9-305, MCA, requires that the state "provide for the immunization, defense and indemnification of its public officers and employees civilly sued for their actions taken within the course and scope of their employment". The University also has commercial coverage for other risk exposures that are not covered by the State's self-insurance program.

Buildings and contents – are insured for replacement value. For each loss covered by the state's self-insurance program and commercial coverage, the University has a \$1,000 per occurrence retention.

General liability and tort claim coverage – include comprehensive general liability, auto liability, personal injury liability, officer's and director's liability, professional liability, aircraft liability, watercraft liability, leased vehicles and equipment liability, and are provided for by the University's participation in the state's self-insurance program.

Self-Funded Programs – The University's health care program is self-funded, and is provided through participation in the Montana University System (MUS) Inter-unit Benefits Program. The MUS program is funded on an actuarial basis and the University believes that sufficient reserves exist to pay run-off claims related to prior years, and that the premiums and University contributions are sufficient to pay current and future claims.

Notes to the Consolidated Financial Statements (continued)

Effective July 1, 2003, (for fiscal year 2004), the University's workers' compensation program became self-funded and is provided through membership in the MUS Self Insured Workers' Compensation Program. In fiscal year 2003 the University's workers' compensation coverage was provided for through participation in the state's Compensation Insurance Fund. The MUS self-funded program is funded on an actuarial basis and is administered by a third party, currently Missoula County. The MUS program incorporates a self-insured retention of \$500,000 per claim and excess commercial coverage to statutory limits. Employer's liability is provided with a \$500,000 retention and an excess insurance limit of \$1,000,000. The University provides periodic disbursements to the administrator for claims paid and administrative expenses. Benefits provided are prescribed by state law and include biweekly payments for temporary loss of wages as well as qualifying permanent partial and permanent total disability. Medical and indemnity benefits are statutorily prescribed for qualifying job-related injuries or illnesses.

NOTE 15 – COMMITMENTS AND CONTINGENCIES

At June 30, 2007, the University had the following outstanding commitments under major capital and maintenance projects:

Project	Budget Authorization	Total Expenditures through June 2007	Funding Source
Skaggs Building Addition	\$ 14,017,000	\$13,962,154	2004 Series I Revenue Bonds, Donations, Grants
Chemistry Building Renovation	825,000	823,824	General Operating and Plant Funds, Donations
Journalism Building	12,050,000	10,200,278	Intercap Loan, Donations and Plant Funds
Law School Expansion	14,900,000	552,109	Donations
Research Facility	11,850,000	1,093,703	2005 Series J Revenue Bonds
Dormitory Sprinkler System	550,000	290,174	2005 Series J Revenue Bonds and Plant Funds
MGBM & Petroleum Building	17,400,000	447,718	Long Range Building Plan and Plant Funds
HPER Building Projects	812,000	18,868	Donations, Plant Funds
Biomass Energy System	1,462,846	1,421,493	Federal Grant and State Bond Proceeds
Auxiliary Steamline	1,795,000	126,364	2005 Series J Revenue Bonds
Upgrade Boiler Controls	253,795	250,495	General Operating and Plant Funds
Curry Health Center HVAC	589,468	548,588	Auxiliary, Plant, and Designated Funds
COT Futures Park	100,000	95,000	Research & Development
Science Complex Network Maintenance	158,000	157,499	Technology Fees
Const Research Lab Fac	1,896,341	1,888,620	Intercap, Auxiliary
Washington-Grizzly Stadium East Expansion	5,500,000	124,966	State, Plant, Donations
	<u>\$ 84,159,450</u>	<u>\$ 32,001,853</u>	

Operating leases – The University has commitments under non-cancelable operating leases as follows:

Payable during the year ending June 30,	Total
2008	\$ 192,839
2009	59,288
2010	35,932
2011	29,007
2012	17,716
	<u>\$ 334,782</u>

The University is a defendant in several legal actions. While the outcome cannot be determined at this time, management is of the opinion that the liability, if any, from these actions will not have a material effect on the University's financial position.

In the normal course of operations, the University receives grants and other forms of reimbursement from various federal and state agencies. These funds are subject to review and audit by the cognizant agencies. The University does not expect any material adjustments or repayments to result from such audits.

Although the University is exempt from federal income tax as an instrumentality of the State of Montana, certain income may be considered unrelated business income by the Internal Revenue Service (IRS). The Montana University System files appropriate tax returns with the IRS to report such income. Because the tax liability for the System as a whole is not material, no provision is recorded in the accompanying consolidated financial statements.

NOTE 16- RELATED PARTIES

The University of Montana is a component unit of the State of Montana. The University's consolidated financial statements and the combined financial statements of its component units include only the activities, funds and accounts of the University and the component units. Private nonprofit organizations with relations to the University include The University of Montana Alumni Association, the Montana Technology Enterprise Center (MonTEC), the Montana Tech Booster Club, the Montana Tech Alumni Association and the University of Montana – Western Booster Club.

The associations and booster clubs operate exclusively for the purposes of encouraging, promoting and supporting educational programs, research, scholarly pursuits and athletics at, or in connection with the University. For the years ended June 30, 2007 and 2006, the following was transferred from or expended by booster clubs for scholarships and construction projects: from the Montana Tech Booster Club \$68,590 and \$53,862, respectively; and \$57,964 and \$78,503 respectively from the University of Montana – Western Booster Club. In exchange, the University provides the associations and booster clubs with office space, staff and some related office expenses.

MonTEC was established as a nonprofit 501 (c) 3 corporation in fiscal year 2001 as a result of an agreement between the University and the Missoula Area Economic Development Foundation (MAEDF). MonTEC provides low cost lease space and business consulting to local "start-up" companies. The corporation's board of directors is comprised equally of members appointed by MAEDF and the University.

NOTE 17 - ACCOUNTING FOR COMPONENT UNITS

The entities included as component units in the financial statements are nonprofit, tax exempt organizations operating exclusively for the purposes of encouraging, promoting and supporting educational programs, research, scholarly pursuits and athletics at, or in connection with the University. Although the University does not control the timing or amount of receipts from these entities, the majority of the revenues or income that the entities hold and invest is restricted to the activities of the University by donors. The entities included as component units in the financial statements are The University of Montana Foundation, The Montana Tech Foundation, The University of Montana – Western Foundation and The Montana Grizzly Scholarship Association.

For the fiscal years ended June 30, 2007 and 2006, the following was transferred to the University for scholarships, academic or institutional support or capital expenses by the University foundations: \$ 13,769,372 and \$12,626,150, respectively with The University of Montana Foundation (406-243-2593), \$ 1,406,888 and \$1,407,020, respectively with the Montana Tech Foundation (406-496-4532); and \$ 315,428 and \$233,928 respectively with The University of Montana-Western Foundation (406-683-7305). In addition, \$1,193,880 and \$1,010,755 was transferred from the Montana Grizzly Scholarship Association (406-243-6485) for the fiscal years ended June 30, 2007 and 2006, respectively. For the fiscal years ended June 30, 2007 and 2006, the University foundations also expended \$5.5 million and \$3.5 million, respectively, directly to third parties in support of the University. In exchange, the University provides the foundations with office space and an annually contracted fee, and the association with office space, staff and some related office expenses. For the fiscal years ended June 30, 2007 and 2006, the University provided \$371,500 and \$332,820, respectively, to its Foundations, which included payments for contracted services and capital campaign support.

Notes to the Consolidated Financial Statements (continued)

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Condensed financial information for each of the University's component units is presented below. The information for The University of Montana – Western Foundation is as of December 31, for the years presented. The financial information for all the other component units is as of June 30, for the years presented.

STATEMENT OF FINANCIAL POSITION June 30, 2007 and December 31, 2006

	University of Montana Foundation *	Montana Tech Foundation *	University of Montana – Western Foundation **	Montana Grizzly Scholarship Association*	Total
ASSETS					
Cash and investments	\$ 161,413,732	\$ 27,940,116	\$ 4,294,203	\$ 1,919,732	\$195,567,783
Other receivables, net of allowances	14,674,705	1,624,575	3,190	86,541	16,389,011
Fixed assets, net of depreciation	4,501,527	202,486	-	5,337	4,709,350
Other assets	599,003	5,722	-	102,022	706,747
	<u>\$ 181,188,967</u>	<u>\$ 29,772,899</u>	<u>\$ 4,297,393</u>	<u>\$ 2,113,632</u>	<u>\$217,372,891</u>
LIABILITIES AND NET ASSETS					
Current liabilities associated with operations	\$ 138,577	\$ 25,667	\$ 14,238	\$ 1,701	\$ 180,183
Note payable – other	338,573	231,300	40,000	-	609,873
Long-term liabilities - other	179,168	57,453	-	247,319	483,940
Liabilities to external beneficiaries	2,904,226	-	-	-	2,904,226
Custodial funds	24,353,157	-	-	-	24,353,157
	<u>27,913,701</u>	<u>314,420</u>	<u>54,238</u>	<u>249,020</u>	<u>28,531,379</u>
Net assets – unrestricted	6,720,732	3,236,158	267,574	950,771	11,175,235
Net assets – restricted	146,554,534	26,222,321	3,975,581	913,841	177,666,277
	<u>153,275,266</u>	<u>29,458,479</u>	<u>4,243,155</u>	<u>1,864,612</u>	<u>188,841,512</u>
	<u>\$ 181,188,967</u>	<u>\$ 29,772,899</u>	<u>\$ 4,297,393</u>	<u>\$ 2,113,632</u>	<u>\$217,372,891</u>

* For the year ended June 30, 2007

** For the year ended December 31, 2006

STATEMENT OF FINANCIAL POSITION June 30, 2006 and December 31, 2005

	University of Montana Foundation *	Montana Tech Foundation *	University of Montana – Western Foundation **	Montana Grizzly Scholarship Association*	Total
ASSETS					
Cash and investments	\$ 139,056,228	\$ 22,572,158	\$ 3,836,474	\$ 1,438,834	\$166,903,694
Other receivables, net of allowances	17,000,021	814,894	-	88,394	17,903,309
Fixed assets, net of depreciation	4,744,545	197,595	-	7,194	4,949,334
Other assets	466,311	5,393	-	46,528	518,232
	<u>\$ 161,267,105</u>	<u>\$ 23,590,040</u>	<u>\$ 3,836,474</u>	<u>\$ 1,580,950</u>	<u>\$190,274,569</u>
LIABILITIES AND NET ASSETS					
Current liabilities associated with operations	\$ 230,235	\$ 18,125	\$ 5,827	\$ 187,848	\$ 442,035
Note payable – other	429,614	129,372	40,000	-	598,986
Long-term liabilities - other	-	75,712	-	-	75,712
Liabilities to external beneficiaries	2,786,406	-	-	-	2,786,406
Custodial funds	19,582,375	-	-	-	19,582,375
	<u>23,028,630</u>	<u>223,209</u>	<u>45,827</u>	<u>187,848</u>	<u>23,485,514</u>
Net assets – unrestricted	6,640,375	3,057,125	246,992	506,314	10,450,806
Net assets – restricted	131,598,100	20,309,706	3,543,655	886,788	156,338,249
	<u>138,238,475</u>	<u>23,366,831</u>	<u>3,790,647</u>	<u>1,393,102</u>	<u>166,789,055</u>
	<u>\$ 161,267,105</u>	<u>\$ 23,590,040</u>	<u>\$ 3,836,474</u>	<u>\$ 1,580,950</u>	<u>\$190,274,569</u>

* For the year ended June 30, 2006

** For the year ended December 31, 2005

STATEMENT OF ACTIVITY
For the year ended June 30, 2007 and December 31, 2006

	University of Montana Foundation *	Montana Tech Foundation *	University of Montana – Western Foundation **	Montana Grizzly Scholarship Association *	Total
REVENUES					
Contributions	\$ 13,885,291	\$ 4,343,065	\$ 551,772	\$ 1,381,127	\$ 20,161,255
Investment income and unrealized gain(loss) of investments	17,775,244	3,834,399	446,249	76,142	22,132,034
Loss on impairment of asset	(166,170)	-	-	-	(166,170)
Contract for services	278,000	222,870	145,405	568,578	1,214,853
Loss on sale of assets	-	(33,500)	-	-	(33,500)
Other income	857,973	2,776	21,900	-	882,649
	\$ 32,630,338	\$ 8,369,610	\$ 1,165,326	\$ 2,025,847	\$ 44,191,121
EXPENSES					
Program services	\$ 13,769,372	\$ 1,406,888	\$ 409,840	\$ 1,193,880	\$ 16,779,980
Supporting services	3,456,529	871,074	302,978	360,457	4,991,038
	\$ 17,225,901	\$ 2,277,962	\$ 712,818	\$ 1,554,337	\$ 21,771,018
Change in net assets before non- operating items	\$ 15,404,437	\$ 6,091,648	\$ 452,508	\$ 471,510	\$ 22,420,103
NONOPERATING EXPENSES					
Payments to beneficiaries and change in liabilities due to external beneficiaries	(367,646)	-	-	-	(367,646)
Change in net assets	15,036,791	6,091,648	452,508	471,510	22,052,457
Net assets, beginning of fiscal year	\$ 138,238,475	\$ 23,366,831	\$ 3,790,647	\$ 1,393,102	\$ 166,789,055
Net assets, end of fiscal year	\$ 153,275,266	\$ 29,458,479	\$ 4,243,155	\$ 1,864,612	\$ 188,841,512

* For the year ended June 30, 2007

** For the year ended December 31, 2006

STATEMENT OF ACTIVITY
For the year ended June 30, 2006 and December 31, 2005

	University of Montana Foundation *	Montana Tech Foundation *	University of Montana – Western Foundation **	Montana Grizzly Scholarship Association *	Total
REVENUES					
Contributions	\$ 18,837,004	\$ 2,276,408	\$ 453,375	\$ 1,413,584	\$ 22,980,371
Investment income and unrealized gain(loss) of investments	10,298,376	1,488,727	138,263	11,956	11,937,322
Contract for services	278,000	260,325	155,773	450,938	1,145,036
Other income	658,991	10,695	41,575	-	711,261
	\$ 30,072,371	\$ 4,036,155	\$ 788,986	\$ 1,876,478	\$ 36,773,990
EXPENSES					
Program services	\$ 15,435,500	\$ 1,407,020	\$ 392,177	\$ 1,010,755	\$ 18,245,452
Supporting services	3,105,934	694,750	185,916	492,052	4,478,652
	\$ 18,541,434	\$ 2,101,770	\$ 578,093	\$ 1,502,807	\$ 22,724,104
Change in net assets before non- operating items	\$ 11,530,937	\$ 1,934,385	\$ 210,893	\$ 373,671	\$ 14,049,886
NONOPERATING REVENUES (EXPENSES)					
Payments to beneficiaries and change in liabilities due to external beneficiaries	(690,566)	-	-	-	(690,566)
Change in net assets	10,840,371	1,934,385	210,893	373,671	13,359,320
Net assets, beginning of fiscal year	\$ 127,398,104	\$ 21,432,446	\$ 3,579,754	\$ 1,019,431	\$ 153,429,735
Net assets, end of fiscal year	\$ 138,238,475	\$ 23,366,831	\$ 3,790,647	\$ 1,393,102	\$ 166,789,055

* For the year ended June 30, 2006

** For the year ended December 31, 2005

The following table shows the total investments held by the component units. The investments for The University of

Notes to the Consolidated Financial Statements (continued)

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Montana – Western Foundation are as of December 31, 2006 and 2005. The financial information for all the other component units is as of June 30, 2007 and 2006.

	Fair Market Value	
	2007	2006
Investments held by component units:		
Stocks and bonds	\$ 175,089,121	\$ 145,054,040
Money market and certificates of deposit	8,772,340	10,895,232
Real property	542,526	542,526
Other	517,510	336,145
	<u>\$ 184,921,497</u>	<u>\$ 156,827,943</u>

Notes to the Consolidated Financial Statements (continued)

NOTE 18 – NATURAL CLASSIFICATION WITH FUNCTIONAL CLASSIFICATIONS

The University's operating expenses by natural and functional classifications for the year ended June 30, 2007, were as follows:

Functional Classification:	Natural Classification						
	Compensation & benefits	Supplies & other services	Utilities	Communication	Scholarships	Depreciation	Total
Instruction	\$ 83,597,918	\$ 6,814,573	\$ 16,655	\$ 465,809	\$ -	\$ -	\$ 90,894,955
Research	31,831,937	15,771,809	77,266	241,481	-	-	47,922,493
Public service	8,004,926	3,829,689	525	81,269	-	-	11,916,409
Academic support	16,140,162	6,174,190	-	308,649	-	-	22,623,001
Student services	13,158,939	8,478,985	6,554	403,469	-	-	22,047,947
Institutional support	16,955,670	6,563,329	220	893,578	-	-	24,412,797
Operation and maintenance of plant	10,387,880	5,605,502	5,500,249	138,962	-	-	21,632,593
Scholarships and fellowships	-	-	-	-	16,355,573	-	16,355,573
Auxiliary enterprises	21,097,536	11,007,583	3,315,087	382,714	-	-	35,802,920
Depreciation	-	-	-	-	-	16,842,365	16,842,365
	\$ 201,174,968	\$ 64,245,660	\$ 8,916,556	\$ 2,915,931	\$ 16,355,573	\$ 16,842,365	\$ 310,451,053

The University's operating expenses by natural and functional classifications for the year ended June 30, 2006, were as follows:

Functional Classification:	Natural Classification						
	Compensation & benefits	Supplies & other services	Utilities	Communication	Scholarships	Depreciation	Total
Instruction	\$ 80,282,745	\$ 7,975,449	\$ 9,987	\$ 429,664	\$ -	\$ -	\$ 88,697,845
Research	29,848,674	16,720,458	116,864	237,711	-	-	46,923,707
Public service	7,578,315	3,243,740	-	86,339	-	-	10,908,394
Academic support	14,386,404	5,848,594	-	255,738	-	-	20,490,736
Student services	12,201,060	7,659,928	7,587	381,472	-	-	20,250,047
Institutional support	15,641,486	6,437,828	73	664,322	-	-	22,743,709
Operation and maintenance of plant	9,804,566	4,387,456	5,307,416	382,155	-	-	19,881,593
Scholarships and fellowships	-	-	-	-	14,682,460	-	14,682,460
Auxiliary enterprises	19,864,853	10,023,681	3,252,037	357,206	-	-	33,497,777
Depreciation	-	-	-	-	-	16,710,382	16,710,382
	\$ 189,608,103	\$ 62,297,134	\$ 8,693,964	\$ 2,794,607	\$ 14,682,460	\$ 16,710,382	\$ 294,786,650

The University of Montana

Supplemental Information - All Campuses

(Unaudited)

<u>DESCRIPTION</u>	<u>Fall 2006</u>	<u>Fall 2005</u>	<u>Fall 2004</u>	<u>Fall 2003</u>	<u>Fall 2002</u>
Enrollment (Headcount) ¹	18,383	17,919	17,796	17,595	17,175
	<u>FY2007</u>	<u>FY2006</u>	<u>FY2005</u>	<u>FY2004</u>	<u>FY2003</u>
Enrollment (FTE) ²					
Colleges of Technology	2,121	2,055	1,881	1,905	1,858
Undergraduate	12,167	11,985	12,026	12,149	12,052
Graduate	1,777	1,747	1,765	1,772	1,630
Enrollment (FTE) ²					
In-State students	12,354	12,215	12,225	12,402	12,070
Out-of-State students	2,732	2,710	2,675	2,699	2,901
Western Undergraduate Exchange	979	862	772	725	569
	<u>FY2007</u>	<u>FY2006</u>	<u>FY2005</u>	<u>FY2004</u>	<u>FY2003</u>
Employees (FTE) - All Funds ³					
Contract Faculty	1,003	993	985	961	937
Contract Admin & Professional	455	386	401	390	366
Classified	1,294	1,283	1,275	1,265	1,266
GTA/GRA	170	173	178	167	170
Part Time and Other	399	403	385	360	378
	<u>6/30/2007</u>	<u>6/30/2006</u>	<u>6/30/2005</u>	<u>6/30/2004</u>	<u>6/30/2003</u>
Degrees Granted ⁴					
Certificate	163	102	76	47	79
Associate	481	478	467	510	492
Undergraduate	2,074	2,034	2,192	2,242	2,136
Graduate	705	711	698	673	620

¹ Source: MUS Data Warehouse

² Source: Internal management reports 2000-2001, CHE Operating Reports 2002-2007

³ Source: CHE Operating Reports 2000-2007

⁴ Source: IPEDS Completion Reports, Fall 2000-2005, internal management reports



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26 November 2007

Mr. Scott A. Seacat
Legislative Auditor
Legislative Audit Division
Room 135 State Capitol
P. O. Box 201705
Helena, MT 59620-1705

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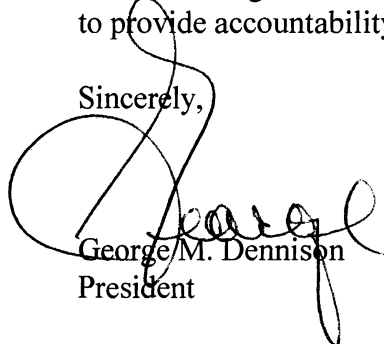
LEGISLATIVE AUDIT DIV.

Dear Mr. Seacat:

We thank the Legislative Audit staff for the cooperation and effort devoted to The University of Montana Financial Audit for the 2007 Fiscal Year. We found the audit team professional and cooperative at all times. The financial audit has become an efficient means to provide the public with an accounting of The University of Montana, and we very much appreciate it.

Thank you and the staff very much for the cooperative efforts. Please convey to the staff members our gratitude for the assistance. We will continue to make improvements and strive to provide accountability in all aspects of our operations.

Sincerely,



George M. Dennison
President

GMD/cc
Denlet3625

c: S. Stearns, Commissioner of Higher Education